Petition

81-1998

No.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

PRICE WATERHOUSE,

Petitioner,

v.

ZELDA L. PANZIRER,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Question Presented

Can a Rule 10b-5 defendant, which has made an allegedly misleading statement relating to an issuer, be held liable to an individual who purchases the issuer's securities in the open market on the basis of comments "heard on the street," as reported in a newspaper article that refers to the issuer but not to the defendant, the defendant's statement or any facts set forth therein?

List of Parties

The parties to the proceedings below were petitioner Price Waterhouse (defendant-appellee below); Emanuel L. Wolf, Jay N. Feldman, C. Ray Holloway, William V. Lurie, Carl Prager, Julio Proietto and Jack M. Sattinger (defendants-appellees below); and respondent Zelda L. Panzirer (plaintiff-appellant below). Petitioner Price Waterhouse is a partnership.

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v.

ZELDA L. PANZIRER,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Price Waterhouse petitions this Court for a writ of certiorari to review the judgment herein of the United States Court of Appeals for the Second Circuit.

Opinions Below

The opinion of the Court of Appeals, reported at 663 F.2d 365 (2d Cir. 1981) *sub. nom. Panzirer* v. *Wolf*, is set forth in the Appendix hereto at 1a-9a. The opinions of the United States District Court for the Southern District of New York, reported at [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,363 and ¶ 97,251 (S.D.N.Y. 1980), are set forth in the Appendix at 16a-37a and 40a-49a.

Jurisdiction

The judgment of the Court of Appeals was entered on October 28, 1981 (10a). Respondent's petition for rehear-

ing was denied by that court on January 28, 1982 (12a). The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

Statute and Rule Involved

Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j (1981), provides:

> "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—
>
> * * * *
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

Rule 10b-5 promulgated by the Securities and Exchange Commission, 17 C.F.R. § 240.10b-5 (1981), provides:

> "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange,
>
> (1) to employ any device, scheme, or artifice to defraud,
>
> (2) to make any untrue statement of a material fact or to omit to state a material fact necessary in

order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security."

Statement of the Case

Price Waterhouse is a firm of independent accountants, performing audits and providing accounting services for individuals, corporations and other entities. Allied Artists Industries, Inc. ("Allied") is a company that at all relevant times was involved in a number of businesses including the production and distribution of motion pictures.* Price Waterhouse audited and expressed a qualified opinion on the financial statements of Allied for the fiscal year ended March 31, 1978 (4a). Respondent Zelda Panzirer purchased common stock of Allied on September 29, 1978 (4a), in the circumstances described below.

A. Allied's 1978 Annual Report

Allied's 1978 Annual Report, which contained allegedly misleading financial statements for fiscal 1978, was dated August 18, 1978 and was mailed to shareholders of record commencing on September 8, 1978 (4a-5a). The auditors' opinion included in the 1978 Annual Report was the only "statement" made by Price Waterhouse concerning Allied. Because of uncertainty concerning the income from one of Allied's major motion pictures, Price Waterhouse qualified

* The seven individual defendants in this action were officers and directors of Allied.

its opinion on the Allied financial statements for fiscal 1978.*

B. Allied's Prospective Entry Into the Video Cassette Market and the "Heard on the Street" Column in The Wall Street Journal

After the close of its fiscal year ended March 31, 1978, Allied publicly announced that, for the first time, it would enter a new product market, the production and distribution of video cassettes (5a). The financial statements audited by Price Waterhouse did not refer or relate to the video cassette business, which Allied had not been engaged in at the end of fiscal 1978. Price Waterhouse did not make any "statement" about Allied's entry into this new market.

On September 29, 1978, a regular column in The Wall Street Journal—"Heard on the Street"—dealt with the video cassette market. The only subject discussed in the column, which is set forth in full at 51a, was the nascent video cassette market and its future prospects. The column mentioned many companies and included the following two paragraphs about Allied:

> "Several analysts contend that Allied Artists is in a good position to take advantage of the growing demand for video tapes, having pioneered the development of pre-recorded cassettes.
>
> Andrew G. Racz of Philips, Appel & Walden, Inc. says Allied Artists, besides having a head start in video tapes and cassettes, is negotiating with TV networks, other film producers and makers of educational films to put their films on video cassettes.

* The financial statements also showed that Allied's current liabilities exceeded its current assets, that there was an accumulated deficit of almost four times Allied's net worth, that Allied had had its third consecutive year of operating losses, and that Allied was six months overdue on over $900,000 in bank debt.

> 'The educational and informational area constitutes a tremendous market for video cassettes,' says Mr. Racz, adding: 'We continue to be bullish on Allied Artists. It's an attractive, turnaround situation.' "

The "Heard on the Street" column did not mention or refer to Allied's 1978 Annual Report, Allied's financial statements or Price Waterhouse.

C. Respondent's Reading of the Wall Street Journal Column and Her Purchase of Allied Stock

While driving with her husband to Vermont, respondent read the "Heard on the Street" column about the video cassette market (3a). Respondent's husband thereupon stopped the car at a gas station, and respondent telephoned her broker (4a). The telephone conversation between respondent and her broker focused upon the video cassette business (33a). The broker pointed out that neither he nor his firm, E. F. Hutton, followed Allied (4a). After a delay while he glanced at the front side of the Standard & Poor's "tear sheet" on Allied—but did not read, either to himself or to respondent, any financial information about Allied—the broker told respondent that he knew of no negative news about Allied (4a, 18a, 32a-33a). Respondent thereupon ordered 200 shares of Allied's common stock (4a).*

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* During the proceedings before the District Court, respondent offered four different and conflicting versions of the telephone call to her broker (8a). The facts set forth herein are (a) the ones upon which the Court of Appeals relied in developing the theory of liability at issue here, and (b) facts relied upon by the District Court that were neither questioned by the Court of Appeals nor disputed in the record, except insofar as respondent's story in a post-deposition affidavit was directly contrary to her deposition testimony (*see* 34a-35a). Since plaintiff's conduct made her lack of credibility "abundantly clear in the record," the Court of Appeals upheld the District Court's ruling that respondent would not be a proper class representative (8a-9a).

After respondent and her husband resumed their trip to Vermont and discussed the matter further, they stopped at another gas station, where respondent again telephoned her broker and increased her order to 500 shares of Allied's common stock, which the broker duly purchased for her (4a). The price at which the stock traded at the time, and the broker's statements made to respondent, were in the words of the Court of Appeals "merely neutral factors as they presented no impediment to [respondent's] acting on the favorable notice in The Wall Street Journal" (6a).

Prior to respondent's purchase of Allied's stock, the only "statement" made by Price Waterhouse was its qualified opinion on the financial statements of Allied for fiscal 1978. Respondent never saw, read or heard about this "statement" or Allied's allegedly misleading financial statements (2a, 5a, 18a). Respondent never saw, read or heard about Allied's 1978 Annual Report (2a, 5a, 18a).

D. The Allegations of the Complaint Concerning Misrepresentations and Omissions in the Annual Report

In April 1979, Allied sought protection from its creditors under Chapter XI of the Bankruptcy Act. Respondent subsequently commenced the present action against Price Waterhouse and various officers and directors of Allied. The complaint charged that the 1978 Annual Report contained numerous misrepresentations and omissions in violation of Section 10(b) of the 1934 Act and Rule 10b-5. As the court below stated, the principal misrepresentation alleged was the inclusion into income of the entire proceeds from the distribution by Allied of a particular film; and the principal omission alleged was the failure of Price Waterhouse to express a "going concern" qualification in its opinion (instead of or in addition to the qualification that Price Waterhouse did express) (*see* 4a).

E. The Decisions of the District Court

The District Court (Motley, *J.*) issued several decisions, eventually granting the motion of Price Waterhouse for summary judgment and denying respondent's motions for class certification and reconsideration of the denial thereof (38a-39a, 49a). In granting summary judgment, the District Court held (1) that neither respondent nor her broker had ever read Allied's allegedly misleading 1978 Annual Report or the financial information contained in the Standard & Poor's tear sheet, and (2) that respondent had purchased Allied common stock based on the "Heard on the Street" column and her conversation with her broker concerning the video cassette business (18a, 32a-33a). The could held that under the so-called "fraud on the market" theory, petitioner had rebutted any presumption that respondent might have purchased the stock based upon the "integrity of the market" (33a-34a). Since respondent had not shown the requisite reliance and causation elements of a claim for relief under Rule 10b-5, summary judgment was entered in favor of the defendants, including petitioner (*see* 31a-35a).

F. The Decision of the Court of Appeals

Respondent appealed the grant of summary judgment and the denial of class certification. The Court of Appeals, while affirming the denial of class certification, reversed the grant of summary judgment and announced a broad and novel theory of liability.

The Court of Appeals held that respondent's "purchase of Allied stock was caused by her perusal of The Wall Street Journal column" about the video cassette business (6a). Respondent had concededly not read or seen the allegedly misleading financial statements published in the Annual Report, or heard about the contents thereof (from her

broker or otherwise) (2a, 5a). Respondent nevertheless advanced the argument that if the Annual Report had been accurate, the stock analyst quoted in the newspaper might not have favorably mentioned Allied, the column might not have spent two paragraphs on Allied's prospects in the nascent video cassette business, and respondent might not have been led by the article to buy Allied's stock (6a). The Court of Appeals accepted this argument and incorporated it into an unprecedented rule of law:

> "Where the plaintiff acts upon information from those working in or reporting on the securities markets, and where that information is circulated after a material misrepresentation or omission, plaintiff has stated a sufficient claim of reliance on the misrepresentation or omission.
>
> * * * *
>
> [Respondent] did not rely on the integrity of the market price because she did not rely on price, but she did rely on the integrity of the market in producing the information reported in The Wall Street Journal. Just as a material misrepresentation or omission is presumed to affect the price of the stock, so it should be presumed to affect the information 'heard on the street' which led [respondent] to make her losing investment." (6a, 8a).

Reasons for Granting the Writ

Under the rule adopted by the court below, once an accountant (or any other defendant in a Rule 10b-5 case) makes a "statement" about an issuer that includes alleged omissions or misrepresentations, the accountant can be held liable to *anybody* who purchases the issuer's securities on the basis of *any* article or reported opinion about the issuer

in *any* publication even where, as here, the statement reported in the media is entirely separate and distinct in subject matter and content from the accountant's statement. To make a Rule 10b-5 defendant responsible for the opinions of unaffiliated parties which appear in the media, or for opinions and information "heard on the street," would be insupportable in theory and incalculable in impact.

The Court of Appeals' decision conflicts with decisions of other circuits. If left standing, it would significantly expand the scope of liability under the 1934 Act by ignoring the fundamental precepts underlying Rule 10b-5 that have been articulated and reiterated by this Court. It would also, for the first time, give rise to the involuntary participation of the media in securities litigation.

The Decision Below Is Contrary to the Decisions in Other Circuits and the Decisions of This Court

The Court of Appeals' decision would render an accountant, or any other defendant associated with the issuance of information relating to a publicly-traded company, subject to liability under Rule 10b-5 even though a third party's statements—not the defendant's allegedly misleading statements—induced the purchase of securities. Such a result would be contrary to the Congressional scheme of securities regulation, to decisions of other circuits and to decisions of this Court. The single Supreme Court authority relied upon by the Court of Appeals—*Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972)—cannot and does not support the reasoning or the result below.

We emphasize what is *not* involved in this case. The decision below did *not* involve a claim of liability based upon reports in the media repeating, summarizing or refer-

ring to the issuer's allegedly false financial statements or to the independent accountants' opinion thereon. Rather, the decision permitted a claim—against the accountants and various corporate insiders—based on statements by third parties to the press concerning a subject matter (the emerging video cassette market) entirely separate, distinct and different from the allegedly false financial statements and the accountants' opinion thereon.

It is difficult to overestimate the potential breadth of the rule announced by the Court of Appeals. Statements that include information, rumor, advice, opinion and crystal ball gazing about publicly-traded companies are extremely widespread. They appear as news stories in the daily press; as articles ranging from topical events to "think pieces" in weekly publications of general orientation (*e.g., Time, Newsweek*) and business orientation (*e.g., Business Week, Barron's*); as specialized, paid-subscription services (*e.g., Value Line Survey*); as investment letters or reports on in-house research by brokerage houses and investment advisors; and as tips, rumors and speculation circulating within the investment community. They are heard regularly on radio and television (*e.g., Wall Street Week*).

All of the foregoing sources carry the kind of statements that appeared in the "Heard on the Street" column and induced respondent's purchase in the present case. Any such statement, opinion, rumor or tip can induce investment decisions. Many are expressly designed to do so. Under the holding below, accountants and other 10b-5 defendants are faced with discovery, trial and possible civil liability arising from every investment decision based on a third person's statement, as reported in the media or "heard on the street," if the plaintiff merely alleges that the statement was preceded—and thus by hypothesis was influenced in some way—by misleading financial statements

that the plaintiff has never seen or heard. The decision below would permit a 10b-5 action to be maintained upon the mere coincidence in time between the allegedly misleading financial statements and market gossip that persuades an investor to purchase.

A. There Is a Conflict Among the Circuits on the Question Presented

In reaching its decision, the court below cited *Blackie* v. *Barrack*, 524 F.2d 891 (9th Cir. 1975), *cert. denied*, 429 U.S. 816 (1976). *Blackie*, an appeal from the denial of class action certification, announced a so-called "fraud on the market" theory. It held (in the context of the "predominance" requirement of Rule 23(b)) that all open-market securities purchasers (whether or not they had seen the issuer's "statement") may be presumed to have relied on the integrity of the price set by the market and thus, indirectly, to have relied on material representations affecting that price. 524 F.2d at 906-07; 7a-8a.*

By its own admission, the court below has created an "extension" of *Blackie* from reliance on price to reliance on any statement quoted in the media or "heard on the street," thereby exposing accountants to liability at the hands of investors or speculators who are induced to purchase by the statements of third and fourth parties. The opinion below not only "extends" *Blackie;* it is flatly contrary to opinions of the Fifth and Eighth Circuits, and is unsupported by any Court of Appeals' opinion that we have been able to find.

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* Price Waterhouse contends that *Blackie* was incorrectly decided. However, even if *Blackie* were accepted by this Court as a correct statement of substantive law, it would not control the present case because, as the Court of Appeals herein noted, respondent did not rely on price—in other words, petitioner successfully rebutted the *Blackie* presumption (*see* 8a).

In *Shores* v. *Sklar*, 647 F.2d 462 (5th Cir. 1981) (*en banc*), *petition for cert. filed*, 50 U.S.L.W. 3377 (U.S. Nov. 2, 1981) (No. 81-839), all 22 members of the Court of Appeals (both the twelve-judge majority and the ten-judge minority) rejected the principle that a purchaser of securities could recover under Rule 10b-5 for alleged misstatements or omissions in an offering circular, where the purchase had been induced by other factors and the purchaser had never seen, read or heard about the statements in the circular. 647 F.2d at 468-70, 472-73.* Similarly, in *Vervaecke* v. *Chiles, Heider & Co.*, 578 F.2d 713 (8th Cir. 1978), the Eighth Circuit held that a purchaser could not maintain a Rule 10b-5 action where, as here, the purchaser had not read or seen the allegedly misleading statements at issue (which appeared in an offering circular that plaintiff had not read). 578 F.2d at 718-19.

The divisiveness and confusion generated by the "fraud on the market" theory are indicated by the fact that in *Shores*, the Court of Appeals split twelve-to-ten over a very limited application of the theory—an application that has no relevance to the present case. The court below, by contrast, applied and extended the fraud on the market theory without citing either *Shores* or *Vervaecke*.

The divisiveness and confusion are further illustrated by the inconsistency between the decision below and *Wilson* v. *Comtech Telecommunications Corp.*, 648 F.2d 88 (2d Cir. 1981), decided by another panel of the Second Circuit. In *Wilson*, plaintiff purchased the defendant company's securities on the basis of two brokers' recommendations that were made after the company's president had allegedly made

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* The petition for certiorari in *Shores* focuses primarily upon theories of liability that do not apply to the present case and were not discussed by the Court of Appeals below.

earnings projections that had become misleading. Concluding that the brokers' recommendations rather than the president's misleading statements had induced plaintiff's purchases, 648 F.2d at 89, 91-92, 94, the court affirmed the dismissal after trial of plaintiff's Rule 10b-5 claim. The court expressly refused to apply any presumption that plaintiff had relied upon the president's statements, and nowhere suggested that liability might be predicated on the theory that the president's prior misleading statements must have influenced the brokers' subsequent recommendations.

* * * *

The decision below is inconsistent with the results and the reasoning in *Wilson* and *Vervaecke*, inconsistent with the reasoning of the majority and the minority in *Shores*, and an admitted extension of the reasoning and holding in *Blackie*. *Vervaecke* and *Wilson* are themselves inconsistent with the result and reasoning in *Blackie*. *Shores* is in some respects narrower than *Blackie* (*see* 647 F.2d at 470) and, as the dissent notes, in some respects broader than *Blackie* (*see* 647 F.2d at 479). Particularly in view of the sweeping consequences that would attend the adoption of the decision below, we respectfully submit that this Court should resolve the conflicts among the Courts of Appeals.

B. The Decision Is Contrary to Congressional Purpose and the Decisions of This Court

This Court has consistently and repeatedly emphasized that the disclosure provisions of the 1933 and 1934 Acts were designed to protect investors from making investment decisions based on false information supplied *to them* in connection with their purchases or sales. *See, e.g., Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 195-96 (1976). Section 10(b) and Rule 10b-5 implement that policy by proscribing material misrepresentations and omissions in state-

ments made "in connection with the purchase or sale of any security." According to the Senate committee report on the 1934 Act, the purchaser or seller must "show the violation or the fact that the statement was false or misleading, *and that he relied thereon to his damage.*" S. Rep. No. 792, 73d Cong., 2d Sess. 12-13 (1934), *quoted in Ernst & Ernst* v. *Hochfelder*, 425 U.S. at 206 (emphasis added). To create an implied civil liability because of allegedly misleading statements where, as here, the statements were never conveyed to the investor, and were never taken into consideration in making the investment decision, is contrary to the underlying congressional regulatory purpose, which was to foster the making of *informed* investment decisions. *See Shores* v. *Sklar*, 647 F.2d 462, 483 (5th Cir. 1981) (Randall, *J.*, dissenting).

The decision below is also inconsistent with the holdings and analyses of this Court in a series of decisions that have delineated the scope of Rule 10b-5 liability, recognized that Rule 10b-5 actions are susceptible to "a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general," and expressed concern that "the inexorable broadening of the class of plaintiffs who may sue in this area will ultimately result in more harm than good.'" *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 739, 747-48 (1975). *See Ernst & Ernst* v. *Hochfelder*, 425 U.S. at 214 n.33.

In *Blue Chip Stamps*, this Court held that a person could not sue under Rule 10b-5 unless he actually purchased or sold securities (rather than, for example, merely retaining them after reading the allegedly false statements at issue). 421 U.S. at 755. In so holding, the Court indicated its concern over the possible exposure of defendants to liability on the basis of "a claimed reading of information contained in the financial pages of a local newspaper," as distinguished

from a reading of the allegedly misleading statements themselves. 421 U.S. at 746. Liability to purchasers or sellers under the rule announced below would be predicated upon precisely such a general reading of the financial pages.

In *Ernst & Ernst* v. *Hochfelder*, this Court held that a plaintiff must prove that the defendant accounting firm's allegedly misleading opinion was issued with *scienter*, *i.e.*, an intent to deceive, manipulate or defraud the purchaser. 425 U.S. at 193, 199.* Noting that plaintiffs had not relied on either the financial statements in question or the accountants' opinion thereon, the Court warned against extending Rule 10b-5 recovery to individuals who were not foreseeable *users* of the financial statements that were the subject of the accountants' opinion. 425 U.S. at 214 n.33. In the present case, respondent was admittedly not a user of the financial statements.

In *Chiarella* v. *United States*, 445 U.S. 222 (1980), this Court held, in the context of a criminal non-disclosure case, that for Rule 10b-5 to apply there must be a "duty to disclose" arising from either the statute or an established relationship of trust and confidence. 445 U.S. at 228, 230. In the present case, no duty under the statutory scheme ran from the petitioner to the respondent, because the predicate for such a duty—a statement by petitioner that has been conveyed to respondent—did not exist. Nor did any duty run from the petitioner to the author of the "Heard on the Street" column or the broker quoted therein, because the

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* In the present case, *scienter* would have to encompass an intent to deceive the broker on the "street" into making statements, different from those included in the issuer's financial statements or the accountants' opinion, that would be repeated in the press and relied upon by potential purchasers like respondent, who never saw, read or heard about the defendant's allegedly misleading statements. We submit that such an expansive reading of *scienter* would be inappropriate.

author and the broker were not purchasers of Allied's stock. The civil liability of petitioner can be implied only by creating an artificial "duty" of uncertain scope running from the petitioner to the respondent—and to the rest of the investing public—through a broker whose motives and bases for recommending the stock are presumed to relate to the allegedly misleading statements, and then through the media, which has independently selected the newsworthy elements from the statements of one or more brokers. It is alien to the structure of the securities laws to premise a "duty" owing from petitioner to respondent upon the conduct or statements of two layers of unaffiliated third parties.

In short, the decision below is difficult or impossible to reconcile with the recent 10b-5 holdings of this Court. Further, the decision below is inconsistent with the analytical framework of this Court's decisions, which have rejected the extension of implied civil liability to situations not governed by the actual language of Section 10(b) and Rule 10b-5—especially where, as here, such extension would create serious problems of its own. *See Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. 723, 733-34, 739-43, 746-49 (1975); *Santa Fe Industries, Inc.* v. *Green,* 430 U.S. 462, 473, 478-79 (1977). *Cf. Chiarella* v. *United States,* 445 U.S. 222, 234 (1980). This Court's statement in *Ernst & Ernst* v. *Hochfelder,* 425 U.S. at 214 n.33, is particularly applicable to the ruling of the court below: "Acceptance of respondents' view would extend to new frontiers the 'hazards' of rendering expert advice under the [Securities] Acts, raising serious policy questions not yet addressed by Congress."*

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* Since Congress provided to buyers of securities certain express remedies under the Securities Act of 1933, it has been suggested that buyers (as opposed to sellers) should not enjoy an implied right to recover under Section 10(b) of the Securities Exchange Act

(footnote continued on following page)

C. The Decision Would Embroil Third Persons and the Press in Rule 10b-5 Litigation

In addition to creating liability where such liability should not exist, the ruling below would create issues not previously raised in Rule 10b-5 litigation and would extend the litigation to individuals not previously involved. Rule 10b-5 litigation has to date been confined largely to inquiries and factual disputes about the conduct, knowledge, state of mind and intent of the purchaser (or seller) and the author of the allegedly misleading statements. Under the ruling below, the scope of Rule 10b-5 litigation would be substantially extended where purchases of securities are induced by stories in the media or statements "heard on the street."

First, the press and other third parties, although having no direct participation or interest in the underlying securities transaction, would be subject to extensive discovery. Such discovery would concern the circumstances of the statement to the media and the knowledge, state of mind and intent with which it was made. This inquiry would

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(footnote continued from preceding page)

of 1934 if they cannot recover under the 1933 Act. *See, e.g.*, Freeman, *Implied Remedies Under Rule 10b-5: Are They Only for Defrauded Sellers?*, National Law Journal, Dec. 10, 1979, at 26, col. 1; 3 Loss, *Securities Regulation* 1787-91 (2d ed. 1961). In *Herman & MacLean* v. *Huddleston*, 50 U.S.L.W. 3802 (U.S. April 5, 1982) (No. 81-680), this Court granted certiorari to consider whether buyers have an implied right to recover under § 10(b) even though they have an express remedy under § 11 of the 1933 Act.

The decision below, insofar as it establishes a theory of recovery for all open market purchasers—whether or not their purchases are made pursuant to a registration statement, prospectus or oral communication governed by the 1933 Act—has consequences that would extend far beyond *Huddleston*. An analysis of the consequences of implying a right to recovery in the present case would be appropriate not only for the reasons set forth in the body of this petition, but also because determination of the present case together with *Huddleston* would provide the lower courts with guidance on a series of related questions that have provoked extreme confusion and inconsistency.

involve the persons quoted in the press, in order to determine whether the statement was actually made, what was the basis for it, why it was made and whether it was accurately reported.* Depending upon the type of statement and publication, the inquiry would also extend to the press itself, including reporters and perhaps rewrite men or more senior editors. The extent to which the inquiry would touch upon other concerns or policies heretofore virtually unheard-of in securities litigation, such as the First and Fourteenth Amendment considerations involved in *Herbert* v. *Lando*, 441 U.S. 153 (1979), is uncertain.

A second potential impact of the Second Circuit's rule would be the inclusion of the persons quoted, and in some instances the press itself, as parties to Rule 10b-5 litigation. Plaintiffs might include such third persons for offensive reasons; defendants might include them for defensive reasons. To the extent that such third persons were named and sought dismissal, they would be confronted with the "notice pleading" nature of the Federal Rules; the often-used and well-recognized but non-uniform principles involving aiding and abetting and contribution; and the lack of uniformity among the circuits concerning whether and the extent to which allegations of recklessness satisfy the *scienter* requirement of 10b-5, *see Ernst & Ernst* v. *Hochfelder*, 425 U.S. at 185, 193-94 n.12.

These substantive and procedural results of applying the decision below indicate that the theory underlying the decision is unsupportable. It is inappropriate to sanction, as did the court below, broadened 10b-5 liability—based upon third parties' statements to the media—on the unsupported theory that readers of such statements can "rely

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* The court below indicated that such an inquiry would be appropriate (6a).

on the integrity of the market in producing the information reported in The Wall Street Journal . . . ." It is particularly inappropriate to do so where the practical effect of the decision would be to expand the scope of Rule 10b-5 litigation and to require the participation of individuals who were not involved with either the purchases at issue or the underlying and allegedly misleading statements.

D. *Affiliated Ute* Does Not Support the Rule of Law Announced by the Court of Appeals

The Court of Appeals relied on this Court's decision in *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128 (1972), to justify the rule announced below. That decision, however, involved silence in the context of face-to-face transactions giving rise to an affirmative duty to disclose, not the question of whether an accountant, having made statements, is liable for a third or fourth party's statements on other subjects appearing in the media. *Affiliated Ute* does not justify, and certainly does not compel, the rule announced below.

In *Affiliated Ute,* two bank employees, acting in a fiduciary capacity on behalf of the sellers and also as purchasers and market-makers for the securities in question, fraudulently failed to inform the sellers, in face-to-face transactions, (a) that the bank employees stood to gain from the transactions and (b) that a higher price for the securities could be obtained by selling on another market. 406 U.S. at 153. In *Chiarella* v. *United States,* 445 U.S. 222, 229-30 (1980), this Court characterized *Affiliated Ute* as involving silence—refraining from making any statement—in the context of an affirmative duty to speak arising out of a fiduciary relationship of trust and confidence.

In the factual pattern and legal context of *Affiliated Ute,* this Court stated that when a 10b-5 claim involved silence,

"positive proof of reliance is not a prerequisite to recovery" if materiality to the investor can be established. 406 U.S. at 153-54. It distorts *Affiliated Ute* beyond recognition to hold, as did the court below, that under *Affiliated Ute* an accountant, which has issued an opinion on an issuer's financial statements, is liable to a securities purchaser who never sees, reads or hears about the accountant's opinion or the financial statements, who has no business or fiduciary relationship with the accountant, and who purchases the issuer's securities because of statements on other subjects made by third persons unaffiliated with the accountant.

Conclusion

For the reasons set forth above, petitioner Price Waterhouse prays that a writ of certiorari be issued to review the judgment below.

Respectfully submitted,

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Appendix

Opinion of the Court of Appeals
Dated October 28, 1981

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 10
Argued: September 16, 1981

August Term, 1981
Decided: October 28, 1981

Docket No. 80-7827

ZELDA L. PANZIRER,

Plaintiff-Appellant,

—against—

EMANUEL L. WOLF, JAY N. FELDMAN, C. RAY HOLLOWAY, WILLIAM V. LURIE, CARL PRAGER, JULIO PROIETTO, JACK M. SATTINGER and PRICE WATERHOUSE & CO.,

Defendants-Appellees.

Before: LUMBARD and KAUFMAN, *Circuit Judges,* and PIERCE, *District Judge.**

Plaintiff appeals from a decision in the Southern District of New York, Motley, *J.*, denying her petition for class certification and dismissing her suit under § 10(b) and Rule 10b-5 of the Exchange Act, 15 U.S.C. 78j(b), 17 C.F.R. § 240.10b-5, for failure to show reliance on the allegedly fraudulent annual report issued and certified by defendants.

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* Honorable Lawrence W. Pierce, United States District Judge for the Southern District of New York, sitting by designation.

Reversed as to the grant of summary judgment against plaintiff; affirmed as to the denial of class certification.

DANIEL W. KRASNER, ESQ., New York, N.Y. (Wolf Haldenstein Adler Freeman & Herz, New York, N.Y., Fred Taylor Isquith, Esq., of counsel), for Plaintiff-Appellant.

BARTLETT H. MCGUIRE, ESQ., New York, N.Y. (Davis Polk & Wardwell, New York, N.Y., Ogden N. Lewis, Esq., Jamie Stern, Esq., Susan P. Johnston, Esq. of counsel), for Defendant-Appellee Price Waterhouse & Co.

JACOBS PERSINGER & PARKER, New York, N.Y. (Irving Parker, Esq., Joseph N. Salomon, Esq., William Lasher, Esq., of counsel), for Defendants-Appellees Wolf, Feldman, Lurie, Prager, Proietto and Sattinger.

GORDON HURWITZ BUTOWSKY BAKER WEITZEN SHALOV & NEEDELL, New York, N.Y., for Defendant-Appellee Holloway.

LUMBARD, *Circuit Judge*:

Allied Artists Industries, Inc., issued an allegedly false annual report in August 1978. Zelda Panzirer purchased Allied stock thereafter upon reading an article in The Wall Street Journal. She never saw the annual report. When Allied started bankruptcy proceedings in 1979, she sued Allied officers and Price Waterhouse & Co., Allied's accountants, under § 10(b) and Rule 10b-5 of the Exchange Act, 15 U.S.C. § 78j(b), 17 C.F.R. § 240.10b-5. She also sought to represent the class of investors purchasing Allied stock after release of the annual report. The district court, per Motley, *J.*, dismissed Zelda Panzirer's suit on summary judgment and denied class certification on the ground that

she had failed to show that reliance on the annual report caused her loss. We reverse in part and affirm in part. Plaintiff relied on an article in The Wall Street Journal which she claims would have presented the company in a less favorable light had the annual report been accurate. She has stated a causal connection between her loss and the annual report which, on this record, cannot be dismissed on summary judgment. We affirm, however, the denial of class certification as being within the discretion of the district court.

On this appeal from summary judgment, the allegations of the complaint, as supplemented by plaintiff's deposition and numerous affidavits submitted by all parties, describe the story of Zelda Panzirer's losing investment in Allied common stock. She read about Allied in The Wall Street Journal while driving up to Vermont on September 29, 1978. The "Heard on the Street" column in that day's Journal covered the video cassette market, and devoted two paragraphs to Allied:

> Several analysts contend that Allied Artists is in a good position to take advantage of the growing demand for video tapes, having pioneered the development of pre-recorded cassettes.
>
> Andrew G. Racz of Philips, Appel & Walden, Inc. says Allied Artists, besides having a head start in video tapes and cassettes, is negotiating with TV networks, other film producers and makers of educational films to put their films on video cassettes. "The educational and informational area constitutes a tremendous market for video cassettes," says Mr. Racz, adding: "We continue to be bullish on Allied Artists. It's an attractive turnaround situation."

Zelda Panzirer had been a substitute school teacher. The item on the educational use of video cassettes caught her eye. She checked the price of Allied common stock, which was listed on the American Stock Exchange and had traded at between $5 and $6⅛ on September 28. Her husband Leo Panzirer stopped the car. Zelda Panzirer called her broker, Michael Blum, at E. F. Hutton's office in Hackensack, N.J. She asked if there was any negative news about Allied. Blum said that neither he nor E. F. Hutton followed the company, but after several minutes delay and a glance at Standard & Poor's tear sheet on Allied, said there was no negative news. Zelda Panzirer ordered 200 shares of Allied common stock. Later on her trip, after discussing the purchase with her husband, she phoned Blum a second time to raise her order to 500 shares. E. F. Hutton purchased the shares for Zelda Panzirer at a September 29 market price of $7 per share.

The Standard & Poor's tear sheet abstracted information from Allied's annual report for the fiscal year ending March 31, 1978. The report was issued on August 18, 1978, and allegedly contained numerous misrepresentations and omissions. The principal misrepresentation was the report of profits for that year based in part on receipts from Allied's film, "The Betsy." In fact, Allied had to split those receipts with the film's overseas distributor, United Artists, and thus lost money in 1978. The principal omission was the annual report's failure to include a qualification by Allied's accountants stating their doubts as to Allied's ability to function as a going concern.[1] Allied common stock closed at

[1] Plaintiff's amended complaint alleges that Price Waterhouse originally included in its certification of Allied's statements a qualification as to Allied's ability to function as a going concern. The complaint alleges that the qualification was removed from the certification before the annual report was published.

$2⅞ per share the day the annual report was issued. It peaked at $7⅜ per share on October 2, 1978,[2] and declined thereafter. Allied filed a Chapter XI petition in bankruptcy on April 4, 1979.

Zelda Panzirer never saw the annual report. In her complaint, she alleges that she relied on the "integrity of the market." She asserts that the annual report affected the market, and therefore she had relied on the report through her reliance on the integrity of the market. Judge Motley, however, found that plaintiff "primarily" relied on The Wall Street Journal column about Allied's prospects in the video cassette market and that plaintiff placed only secondary reliance on the integrity of the market. She held that secondary reliance was insufficient to support a 10b-5 claim. We cannot agree. We find no support in the law for the district court's distinction between primary and secondary reliance.

The function of requiring the plaintiff to show reliance in a 10b-5 action is to permit only those injured by fraud to sue. If plaintiff can link her injury to defendant's fraud by showing the fraud was a "substantial" or "significant contributing cause," plaintiff has shown sufficient reliance to support her 10b-5 claim. *Wilson* v. *Comtech Telecommunications Corp.*, 648 F.2d 88, 92 (2d Cir. 1981). Plaintiff has on this record stated a sufficient connection between her

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[2] The annual report was not mailed to Allied shareholders until Friday, September 8, on which date Allied common stock closed at $3⅛. Allied's entry into the video cassette market was announced on Saturday, September 9. Whether the subsequent appreciation in price was due to the annual report or to Allied's entry into the video cassette market is irrelevant to our decision, as we do not depend on Zelda Panzirer's knowledge of the market price. Though Michael Blum stated in his affidavit that he mentioned the activity of Allied common to plaintiff, she nowhere refers to the stock's activity as a reason for her purchase.

loss and the allegedly fraudulent annual report to withstand a motion for summary judgment.

As we read the record, Zelda Panzirer's purchase of the Allied stock was caused by her perusal of The Wall Street Journal column. Her knowledge of the price of the stock and her conversation with her broker were merely neutral factors as they presented no impediment to her acting on the favorable notice in The Wall Street Journal.[3] Consequently, the plaintiff argues that if Allied's report had been accurate, the stock analysts interviewed by the Journal would not have mentioned the company favorably, the Journal would not have devoted two paragraphs to Allied's prospects in the video cassette market, and plaintiff would not have been led by the article to buy her stock. Defendants have introduced no evidence to contradict this chain of causation. Though, at trial, the validity of the chain of causation will be tested, on summary judgment questions about this chain of causation must be resolved in favor of plaintiff, who in the case of a material fraud on the market enjoys a presumption of reliance. Where the plaintiff acts upon information from those working in or reporting on the securities markets, and where that information is circulated after a material misrepresentation or omission, plaintiff has stated a sufficient claim of reliance on the misrepresentation or omission.

Our holding is supported by *Competitive Associates, Inc.* v. *Laventhol, Krekstein, Horwath & Horwath,* 516 F.2d 811 (2d Cir. 1976). In that case, investment manager

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[3] Plaintiff refers to the price of Allied common stock once in her deposition: "If the price was outrageous, something very high, I wouldn't have been interested. The price was attractive." If anything, her testimony indicates that a lower price accurately reflecting Allied's true financial position might have led her to buy more stock.

Akiyoshi Yamada mishandled a Competitive Associates' investment fund. Yamada had previously mishandled another investment fund, but his earlier mistakes had been hidden by alledgedly false financial statements certified by the defendant accountants. The district court granted summary judgment to defendants on the ground that because Competitive Associates did not see the financial statements it could not prove reliance on them. We reversed, holding that Competitive Associates need not prove direct reliance, but only causation in fact. That is all Zelda Panzirer need show here. As in *Competitive Associates,* the fact that plaintiff must trace her reliance on defendant's alleged fraud through the reactions of third parties does not vitiate her claim under 10b-5.

Where, as is here alleged, the fraud consists of a failure to disclose, the difficult nature of plaintiff's claim—that if there had been disclosure, plaintiff would not have been harmed—has led the Supreme Court to hold that if the omission is material, reliance upon the omission will be presumed. *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128, 153-54 (1972). Proving reliance is necessarily difficult where the fraud has affected the market and damaged the plaintiff only through its effect on the market. Relying on *Affiliated Ute,* this and other circuits do not require direct reliance where the fraud affects the market, on the ground that the investor relies generally on the supposition that the market price is validly set and that no unsuspected fraud has affected the price. *See Ross* v. *A.H. Robins Co.,* 607 F.2d 545, 554 (2d Cir. 1979), *cert. denied,* 446 U.S. 946 (1980); *Blackie* v. *Barrack,* 524 F.2d 891, 906-07 (9th Cir. 1975), *cert. denied,* 429 U.S. 816 (1976). As in *Affiliated Ute, Blackie* held that the materiality of a fraud creates a presumption of reliance through its pre-

sumed effect on the market. *See also* Note, *The Reliance Requirement in Private Actions Under SEC Rule* 10b-5, 88 Harv. L. Rev. 584, 589 (1975).

Our holding is no more than an extension of *Blackie*. Zelda Panzirer did not rely on the integrity of the market price because she did not rely on price, but she did rely on the integrity of the market in producing the information reported in The Wall Street Journal. Just as a material misrepresentation or omission is presumed to affect the price of the stock, so it should be presumed to affect the information "heard on the street" which led Zelda Panzirer to make her losing investment.

Merely because Zelda Panzirer's own claim survives summary judgment, however, does not make her fit to represent a class of Allied investors. Plaintiff appeals from Judge Motley's denial of class certification. Judge Motley ruled that the weakness of plaintiff's case concerning reliance made her claim atypical under Fed. R. Civ. P. 23(a)(3), and also ruled that plaintiff's lack of credibility made her an inadequate class representative under Fed. R. Civ. P. 23(a)(4). We affirm on the latter ground.[4] Plaintiff's lack of credibility is abundantly clear in the record. She gave no less than four versions of her conversation with her broker. At her deposition, she described the conversation as containing no specific information about Allied. Before signing her deposition, she changed her story to say that Michael Blum had read unspecified information to her from his Standard & Poor's tear sheet. In her affidavit explaining her changes in testimony, she alleged that he had

[4] We do not decide whether Zelda Panzirer's weak showing of reliance makes her claim atypical under Fed. R. Civ. P. 23(a)(3), as we find her numerous changes in her testimony sufficient reason to deny class certification.

told her that Allied had made money in 1978. After defendants introduced an affidavit from the broker that he had never looked at the financial information on Allied in the tear sheet, Zelda Panzirer introduced a final affidavit alleging that he had read financial information to her from the tear sheet. The credibility of a plaintiff may be considered by the trial judge in determining the plaintiff's adequacy as a class representative. *Kline* v. *Wolf*, 88 F.R.D. 696, 699-700 (S.D.N.Y. 1981); C. Wright & A. Miller, Federal Practice & Procedure § 1766 at 632-34. Judge Motley acted well within her discretion in concluding that Zelda Panzirer's lack of credibility rendered her an inadequate class representative.

Affirmed in part, reversed in part; remanded for proceedings consistent with this opinion.

Judgment of the Court of Appeals
Dated October 28, 1981

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

#80-7827

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the twenty-eighth day of October one thousand nine hundred and eighty-one

Present:

HON. J. EDWARD LUMBARD,
HON. IRVING R. KAUFMAN,
Circuit Judges
HON. LAWRENCE W. PIERCE,
District Judge

ZELDA L. PANZIRER,

Plaintiff-Appellant,

v.

EMANUEL L. WOLF, JAY N. FELDMAN, C. RAY HOLLOWAY, WILLIAM V. LURIE, CARL PRAGER, JULIO PROIETTO, JACK M. SATTINGER and PRICE WATERHOUSE, & COMPANY,

Defendants-Appellees.

Appeal from the United States District Court for the Southern District of New York.

Judgment of Court of Appeals

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is reversed in part and affirmed in part in accordance with the opinion of this court.

/s/ A. DANIEL FUSARO
Clerk

/s/ Arthur Heller
by ARTHUR HELLER,
Deputy Clerk

Order of the Court of Appeals Dated January 28, 1982 Denying Petition for Rehearing

At a stated term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse, in the City of New York, on the 28th day of January, one thousand nine hundred and eighty-two.

No. 80-7827

ZELDA L. PANZIRER,

Plaintiff-Appellant,

—against—

EMANUEL L. WOLF, JAY N. FELDMAN, C. RAY HOLLOWAY, WILLIAM V. LURIE, CARL PRAGER, JULIO PROIETTO, JACK M. SATTINGER and PRICE WATERHOUSE & CO.,

Defendants-Appellees.

A petition for rehearing containing a suggestion that the action be reheard en banc having been filed herein by counsel for the plaintiff-appellee, Zelda L. Panzirer,

Upon consideration by the panel that heard the appeal, it is

ORDERED that said petition for rehearing is DENIED.

It is further noted that the suggestion for rehearing en banc has been transmitted to the judges of the court in regular active service and to any other judge on the panel that heard the appeal and that no such judge has requested that a vote be taken thereon.

/s/ A. DANIEL FUSARO
Clerk

Judgment of the District Court (Motley, J.)
Dated September 25, 1980

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

Index No.: 79 Civ. 3445 (CBM)

Received Sep 24 1980 Filed Sep 25 1980

ZELDA L. PANZIRER,

Plaintiff,

—against—

EMANUEL L. WOLF, JAY N. FELDMAN, C. RAY HOLLOWAY, WILLIAM D. LURIE, CARL PRAGER, JULIO PROIETTO, JACK M. SATTINGER and PRICE WATERHOUSE & CO.,

Defendants.

—and—

ROBERT SISK,

Third Party Defendant.

JUDGMENT

This cause having come to be heard before this Court, Honorable Constance Baker Motley, District Judge presiding, upon:

The motion by plaintiff Zelda L. Panzirer for class action determination, pursuant to notice of motion dated November 14, 1979;

The motion by defendant Price Waterhouse & Co. for summary judgment in its favor dismissing the action, pur-

suant to notice of motion dated November 29, 1979;

The motion by defendants Emanuel L. Wolf, Jay N. Feldman, William D. Lurie, Carl Prager, Julio Proietto and Jack M. Sattinger for summary judgment in their favor dismissing the action, pursuant to notice of motion dated November 30, 1979;

The motion of plaintiff Zelda L. Panzirer for leave to reargue the class action determination, pursuant to notice of motion dated January 28, 1980;

The renewed motion of defendant Price Waterhouse & Co. for summary judgment in its favor dismissing the action, pursuant to notice of motion dated February 19, 1980;

The renewed motion of defendants Emanuel L. Wolf, Jay N. Feldman, William D. Lurie, Carl Prager, Julio Proietto and Jack M. Sattinger for summary judgment in their favor dismissing the action, pursuant to notice of motion dated February 19, 1980; and

The motion of defendant C. Ray Holloway for summary judgment in his favor dismissing the action; and

The Court having considered the pleadings in the action, the affidavits, exhibits and other papers submitted by the parties in connection with the above-referenced motions, and the Court having heard the argument of counsel and due deliberation having been heard thereon and a decision having been duly rendered; and

The Court having issued its Order dated January, 1980 and Memorandum Opinion dated January 16, 1980; and

The Court having issued its Order dated April 21, 1980 and its Memorandum Opinion dated April 21, 1980; and

The Court having issued its Order entered September 5, 1980.

Now, it is ORDERED AND ADJUDGED,

Judgment of District Court

That plaintiff Zelda L. Panzirer's action be, and hereby is, dismissed and discontinued.

Dated: New York, New York, this 24th day of September, 1980

CONSTANCE BAKER MOTLEY
U.S.D.J.

JUDGMENT ENTERED 9/25/80

RAYMOND F. BURGHARDT
Clerk

Order of the District Court (Motley, J.)
Dated September 5, 1980

MICROFILM

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

79 Civ. 3445 (CBM)
Filed Sep. 5, 1980

The motion of defendant Holloway for summary Judgment is granted. See the Court's Opinion on motion for summary Judgment made by all other defendants dismissing Complaint. This Action is discontinued and Complaint dismissed.

/s/ .....
CONSTANCE BAKER MOTLEY
U.S.D.J.

Opinion of the District Court (Motley, J.)
Dated April 21, 1980

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

79 Civ. 3445

ZELDA L. PANZIRER,

Plaintiff,

—against—

EMANUEL L. WOLF, JAY N. FELDMAN, C. RAY HOLLOWAY, WILLIAM V. LURIE, CARL PRAGER, JULIO PROIETTO, JACK M. SATTINGER and PRICE WATERHOUSE & CO.,

Defendants.

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Opinion of District Court—April 21, 1980

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CONSTANCE BAKER MOTLEY, D. J.

MEMORANDUM OPINION

Four motions are presently before the court in this action: 1) Plaintiff has moved, pursuant to Rule 9(m) of the General Rules of this Court, for leave to reargue plaintiff's motion for class action certification; 2) plaintiff has moved, alternative pursuant to 28 U.S.C. § 1292(b), for certification of the issue of class adjudication to the Court of Appeals; 3) defendants have moved for an order, pursuant to Rule 56 of the Federal Rules of Civil Procedure, granting summary judgment in favor of defendants; and 4) proposed intervenor Paul Block has moved for an order pursuant to Rule 24 of the Federal Rules of Civil Procedure granting Paul Block leave to intervene and to serve and file his proposed intervenor's complaint.

Background

The amended complaint in this action alleges a violation of section 10(b) of the Securities Exchange Act of 1934,

as amended, 15 U.S.C. § 78j(b), and Rule 10b-5 of the Securities and Exchange Commission's rules and regulations promulgated thereunder, 17 C.F.R. § 240.10b-5. The amended complaint in this action alleges that defendants caused Allied to issue to the investing public false and misleading statements about Allied's financial condition. The allegations relate to Allied's 1978 Annual Report, which included financial statements for the fiscal year ending March 31, 1978.

Plaintiff alleges that in purchasing 500 shares of Allied stock on September 29, 1978, she "relied upon the aforesaid materially false and misleading statements of defendants and/or upon the integrity of the market price of Allied's stock as reflected by the impact of said statements on the market for Allied securities." Plaintiff further alleges that these misrepresentations were part of a scheme to portray falsely Allied's financial condition and to cause Allied's stock to trade at artificially high prices.

On November 6, 1979, plaintiff's deposition was taken by defendants. Plaintiff testified that she was not aware of Allied's financial position at the time she purchased her Allied stock. Plaintiff testified that she did not see a copy of Allied's 1978 Annual Report prior to her purchase of Allied shares on September 28, 1978. In short, plaintiff received no financial information about Allied. Instead, plaintiff testified that she bought Allied stock because of a newspaper article appearing in the *Wall Street Journal* on the day of her purchase, September 29, 1978. Plaintiff testified that she telephoned her broker, who told her that there was no negative news about Allied. Plaintiff testified that other than the newspaper article and the discussion with her broker, she did not rely on any other information about Allied in making her purchase. With respect to the newspaper article, plaintiff testified:

I never knew specifically what Allied Artists did. Of course, the name is known to me as being in the film business. I didn't know of any of their subsidiaries or what other business they were involved in. But this article was very interesting because this Mr. Racz gave a glowing report. He said, "Allied Artists, besides having a head start in videotapes and cassettes, is negotiating with the TV networks, other film producers and makers of educational films"—of course I am involved in educational films, as I am a teacher currently not that active, but we have used so many educational films—"to put their films on video cassettes."

"The educational informational area constitutes a tremendous market for video cassettes, says Mr. Racz, adding: 'We continue to be bullish on Allied Artists. It's an attractive turn-around situation.'" End of quote.

Panzirer dep. at 131-32.

On December 21, 1979, during oral argument before the court, plaintiff's attorney noted that defendants had not submitted plaintiff's deposition to her for examination and signing. It was then agreed that defendants would submit plaintiff's deposition to her sometime following the oral argument.

On January 3, 1980, plaintiff signed her deposition, after making numerous changes in her testimony. Accompanying her signed deposition, as changed, was plaintiff's affidavit which was submitted to explain the "corrections made in [her] deposition transcript prior to the execution thereof."

In her deposition testimony, as "corrected" on January 3, 1980, plaintiff states that her broker read to her from the Standard and Poor's "tear sheet" during their telephone

conversation of September 29, 1978. Plaintiff states in her "corrected" deposition testimony that at the time of purchase she knew only what she read in the newspaper article *and* what her broker told her over the phone. Thus, in her "corrected" deposition testimony, plaintiff states that "[a]side from what [she] testified earlier," she wasn't aware of Allied's financial position at the time she purchased and that "[a]side from what she testified earlier," she received no financial information about Allied from her broker. In short, plaintiff now testifies that she bought Allied stock because of the newspaper article and her discussion with her broker.

Memorandum Opinion of January 16, 1980

On January 16, 1980, the court issued a memorandum opinion denying a motion by defendants for summary judgment, and denying a motion by plaintiff for class certification. In denying defendants' motion for summary judgment, the court noted that the presumption of reliance in a "fraud on the market" case "can be rebutted with proof that the market's integrity and the alleged misrepresentations were not material to plaintiffs or that they relied primarily on another source. *Greenspan* v. *Brassler*, 78 F.R.D. 130, 133 (S.D.N.Y. 1978)." The court then explained:

> In the case at hand, there is a genuine issue as to whether the market's integrity and the alleged misrepresentations were material to plaintiff and whether plaintiff relied primarily on another source. In her deposition testimony, plaintiff stated that she asked her broker if he had heard any negative news about Allied. After the broker told plaintiff that there was no negative news about Allied, plaintiff purchased

> Allied stock. Plaintiff's inquiry to her broker might suggest that the market's integrity *was* material to plaintiff. Moreover, in her "corrected" deposition testimony, plaintiff stated that she bought Allied stock because of the newspaper article *and* her discussion with her broker concerning the Standard and Poor's "tear sheet." This "tear sheet" included financial information concerning Allied which had appeared in the 1978 Annual Report. Given plaintiff's "corrected" deposition testimony, there is a genuine issue as to whether plaintiff relied *primarily* on the newspaper article rather than the market's integrity or the alleged misrepresentations. As recognized above, this court has serious reservations regarding the credibility of plaintiff's changes in her deposition testimony. Nevertheless, these issues are best resolved by the jury at trial. In light of the genuine issue as to plaintiff's reliance, a material fact in this action, defendants motion for summary judgment must be denied.

In denying plaintiff's motion for class certification, the court concluded that plaintiff did not meet the requirement of Rule 23(a)(3), relying upon the court's holding in *Greenspan* v. *Brassler, supra,* where the court held that class status must be denied when the putative representative is subject to unique defenses that will unnecessarily prejudice the class's probability of success. In the case at hand, the court explained:

> Rule 23(a)(3) provides that a prerequisite to a class action is that "the claims or defenses of the representative parties are typical of the claims or defenses of the class." In the case at hand, the record before the court clearly indicates that plaintiff may be

subject to defenses not applicable to other class members. Plaintiff's possible reliance on a newspaper article relating to Allied's video cassette business, rather than on the market's integrity or the alleged misrepresentations in the 1978 Annual Report, raises issues qualitatively different from the questions of individual reliance normally inherent in a fraud on the market suit. Thus, certification of this suit as a class action must be denied since plaintiff is subject to unique defenses that will unnecessarily prejudice the class' probability of success. Although the evidence is insufficient to compel summary judgment in defendants' favor, plaintiff may be subject to the defenses that 1) she relied primarily on a source other than the market's integrity and the alleged misrepresentations; or 2) that the market's integrity and the alleged misrepresentations were not directly material to plaintiff.

Motion to Reargue Class Action Certification

Plaintiff has moved, pursuant to Rule 9(m) of the General Rules of this court, for leave to reargue plaintiff's motion for class certification. It is well-established that the only proper ground for a motion for reargument is that the court has overlooked "matters or controlling decisions" which, had they been considered, might reasonably have altered the result reached by the court. *United States* v. *International Business Machines Corp.*, 79 F.R.D. 412, 414 (S.D.N.Y. 1978). Plaintiff's motion for reargument must be denied, as plaintiff has not set forth any "matters or controlling decisions" which the court has overlooked.

Plaintiff suggests that the court has overlooked the "unique facts" in *Greenspan* v. *Brassler, supra,* which make the case "clearly inapposite." Plaintiff previously attempted

to distinguish *Greenspan* in her briefing on the original class action motion. Plaintiff's renewed attempt to distinguish *Greenspan* is insufficient to create a matter overlooked by the court pursuant to Rule 9(m). In any event, plaintiff's assertion that *Greenspan* is distinguishable, or should be somehow limited to its "unique facts," is simply incorrect.

Plaintiff urges the court, in effect, to limit the applicability of *Greenspan* to cases where: 1) the plaintiff relied on the recommendation of a relative in making her purchase; 2) the plaintiff purchased additional shares of the securities at issue after disclosure of the alleged fraud; 3) the plaintiff was totally inattentive to the conduct of the litigation; and 4) there were serious doubts about the adequacy of plaintiff's counsel. Plaintiff's suggested method of reading *Greenspan* would in effect have this court limit virtually every decision of this court to its facts. Nothing in the court's opinion in *Greenspan* suggests, even vaguely, that the *Greenspan* holding is to be so narrowly construed. The court stated in *Greenspan* that "class status must be denied when, as here, the putative representative is subject to unique defenses that will unnecessarily prejudice the class's probability of success." 78 F.R.D. at 132. The court did not indicate that this holding is limited to situations where a plaintiff has relied on the recommendations of a brother, as plaintiff seemingly implies.

Plaintiff's attempt to distinguish two cases relied upon by the court in its *Greenspan* opinion is equally unpersuasive. In *Kraus* v. *Paterson Parchment Paper Co.*, 65 F.R.D. 368, 369 (S.D.N.Y. 1974), the court denied class certification based, in part, upon the fact that defendants had defenses against the proposed class representative which would not necessarily have been available with respect to members of the class whom the individuals sought

to represent. Similarly, in *Koos* v. *First National Bank of Peoria*, 496 F.2d 1162, 1164 (7th Cir. 1974), the Seventh Circuit held that "[w]here it is predictable that a major focus of the litigation will be on an arguable defense unique to the named plaintiff or a small subclass, then the named plaintiff is not a proper class representative." While the facts in the case at hand may be somewhat different from the facts in *Greenspan*, *Kraus*, or *Koos*, the case at hand is strikingly similar to those cases in that the plaintiff is subject to unique defenses that will unnecessarily prejudice the class's probability of success. While there may exist cases which have allowed class certification in this situation, such cases are contrary to the law of this court as currently reflected in *Greenspan*. *Compare Dorfman* v. *First Boston Corp.*, 62 F.R.D. 466, 472 (E.D. Pa. 1974), *with Zenith Laboratories, Inc.* v. *Carter-Wallace, Inc.*, 530 F.2d 508, 512 (3d Cir.), *cert. denied*, 429 U.S. 828 (1976) ("Since these unique defenses could conceivably become the focus of the entire litigation and divert much of [plaintiff's] attention from the suit as a whole, the remaining members of the class could be severely disadvantaged by [plaintiff's] representation.").

Plaintiff also suggests that the court has overlooked the possibility that *Greenspan* was wrongly decided. Plaintiff previously attempted to argue against the *Greenspan* position in her briefing on the original class action motion. Plaintiff's renewed attempt to raise similar arguments against the court's position, as articulated in *Greenspan*, is insufficient to create controlling decisions overlooked by the court pursuant to Rule 9(m). In any event, plaintiff's assertion that *Greenspan* was wrongly decided, or is inconsistent with Supreme Court or Second Circuit decisions, is without merit.

Plaintiff is correct to the extent that she asserts that "[i]n determining the propriety of a class action, the question is not whether the plaintiff or plaintiffs have stated a cause of action or will prevail on the merits, but rather whether the requirements of Rule 23 are met." *Eisen* v. *Carlisle & Jacquelin*, 417 U.S. 156, 178 (1974). Nevertheless, it is well-established that "the class determination generally involves considerations that are 'enmeshed in the factual and legal issues comprising the plaintiff's cause of action.'" *Coopers & Lybrand* v. *Livesay*, 437 U.S. 463, 469 (1978). Contrary to plaintiff's characterization the court's *Greenspan* holding endorsed an inquiry into whether the typicality requirement of Rule 23(a)(3) had been met, not whether plaintiffs have stated a cause of action or will prevail on the merits. In both *Greenspan* and in the case at hand, the court is engaging in a class determination which, quite properly, involves considerations that are enmeshed in the factual and legal issues comprising the plaintiff's cause of action.

Plaintiff is also correct to the extent that she asserts that the trial court can order separate trials on the issue of individual reliance. *See Green* v. *Wolf Corp.*, 406 F.2d 291, 301 (2d Cir. 1968), *cert. denied*, 395 U.S. 977 (1969). While the possibility of separate trials might allow a plaintiff to satisfy the Rule 23(b)(3)'s requirement of "predominance of common questions," the possibility of separate trials does little, if anything, to satisfy Rule 23(a)(3)'s typicality requirement. In part, the rationale of the *Greenspan* rule is that the unique defenses against the plaintiff could divert much of the plaintiff's attention from the suit as a whole, thus severely disadvantaging the remaining members of the class. *See Zenith Laboratories, Inc.* v. *Carter-Wallace, Inc.*, *supra*, 530 F.2d at 512. While

dismissal on the merits of the class representative's individual claim after trial will not necessarily preclude class recovery, the class may nonetheless be severely prejudiced by the representation of a plaintiff preoccupied with dealing with unique defenses.

The numerous cases offered by plaintiff do not constitute controlling decisions which indicate that *Greenspan* was wrongly decided. In *Korn* v. *Franchard Corp.*, 456 F.2d 1206, 1211 (2d Cir. 1972), for example, the Second Circuit found that the record before the court provided "too feeble a foundation for considering [plaintiff] atypical or unrepresentative on the ground of her lack of reliance." The Second Circuit did not preclude a finding that a plaintiff was atypical or unrepresentative in other cases, such as the present case, where the record was sufficient to support such a finding. In *Greene* v. *Emersons, Ltd.*, [Current] CCH Fed. Sec. L. Rep. ¶ 97,267, at 96,881 (S.D.N.Y. Jan. 30, 1980), the court recently reviewed its *Greenspan* holding. The court explained that in *Greenspan*, plaintiffs' position differed so fundamentally from that of purchasers who relied solely upon market performance, as revealed in public documents, that they could not act as effective representatives of such a class. Thus, *Greene* simply reaffirms the applicability of *Greenspan* to the case at hand, where the record suggests that plaintiff is subject to the unique defense that she did not rely upon market performance in her purchase of Allied stock. *See also In re Commonwealth Oil/Tesoro Petroleum*, MDL No. 347 (W.D. Tex. July 26, 1979); *Sicinski* v. *Reliance Funding Corp.*, 82 F.R.D. 730, 733-34 (S.D.N.Y. 1979); *Tanzer* v. *Sharon Steal Corp.*, [1979 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 96,915, at 95,795-96 (S.D.N.Y., June 22, 1979).

In conclusion, plaintiff has failed to set forth "matters or controlling decisions" overlooked by the court which might reasonably have altered the result reached by the court. Accordingly, plaintiff's motion for reargument pursuant to Rule 9(m) must be denied.

Motion for Certification to the Court of Appeals

Plaintiff has moved, pursuant to 28 U.S.C. § 1292(b), for certification of the issue of class adjudication to the Court of Appeals. Section 1292(b) provides, in pertinent part:

> When a district judge, in making in a civil action an order not otherwise appealable under this section, shall be of the opinion that such order involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation, he shall so state in writing in such order.

The earliest case to analyze Section 1292(b) and its requirement that an appeal "may materially advance the ultimate termination of the litigation" was *Milbert* v. *Bison Laboratories, Inc.*, 260 F.2d 431 (3d Cir. 1958). In *Milbert,* the Third Circuit quoted extensively from the legislative history of Section 1292(b) and concluded that the section "is to be used only in exceptional cases where an intermediate appeal may avoid protracted and expensive litigation and is not intended to open the floodgates to a vast number of appeals from interlocutory orders in ordinary litigation." *Id.* at 433; *accord, Kraus* v. *Board of County Road Commissioners,* 364 F.2d 919 (6th Cir. 1966). Thus, it is clear that "Section 1292(b) was intended pri-

marily as a means of expediting litigation by permitting appellate consideration during the early stages of litigation of legal questions which, if decided in favor of the appellant, would end the lawsuit." *United States* v. *Woodbury*, 263 F.2d 784, 787 (9th Cir. 1959) [footnote omitted]. *See generally* Note, *Interlocutory Appeals in the Federal Courts Under 28 U.S.C. § 1292(b)*, 88 Harv. L. Rev. 607, 612 (1975) ("efficiency is the sole policy guiding application of the Act"); *id.* at 610-12.

The Second Circuit in *Gottesman* v. *General Motors Corp.*, 268 F.2d 194 (2d Cir. 1959), also reviewed the legislative history of Section 1292(b) and reached similar conclusions. In *Gottesman*, the Second Circuit noted "the limited and exceptional character of cases to which [Section 1292(b)] applies" and followed the *Milbert* holding that the court's "power must be strictly limited to the precise conditions stated in the law." *Id.* at 196; *accord*, *Hunt* v. *Mobil Oil Corp.*, 410 F. Supp. 4, 28 (S.D.N.Y. 1975), *aff'd*, 550 F.2d 68 (2d Cir.), *cert. denied*, 434 U.S. 984 (1977). In accordance with the Second Circuit's opinion in *Gottesman*, this court explained in *United States* v. *International Business Machines Corp.*, 406 F. Supp. 184, 185-86 (S.D.N.Y. 1975), that "certification is proper only under the most unusual circumstances where the immediate appeal might avoid protracted and costly litigation." *Accord*, *Bobolakis* v. *Compania Panamena Maritima San Gerassima*, 168 F. Supp. 236, 237 (S.D.N.Y. 1958).

The Supreme Court has held that a district court's determination that an action may not be maintained as a class action is not a "final decision" within the meaning of 28 U.S.C. § 1291 and therefore is not appealable as a matter of right. *Cooper & Lybrand* v. *Livesay*, 437 U.S. 463 (1978). The Court has, however, approved discretionary

appellate review, pursuant to Section 1292(b), of orders denying class certification. *Id.* at 474-75 & n.27. In fact, the Court has quoted approvingly Judge Friendly's opinion in *Parkinson* v. *April Industries, Inc.*, 520 F.2d 650, 660 (2d Cir. 1975) (Friendly, J., concurring):

> [T]he best solution is to hold that appeals from the grant or denial of class action designation can be taken only under the procedure for interlocutory appeals provided by 28 U.S.C. § 1292(b) .... Since the need for review of class action orders turns on the facts of the particular case, this procedure is preferable to attempts to formulate standards which are necessarily so vague as to give rise to undesirable jurisdictional litigation with concomitant expenses and delay.

Coopers & Lybrand v. *Livesay, supra,* 437 U.S. at 475 n.27. *See also Weisman* v. *Darneille,* 78 F.R.D. 671, 673-74 (S.D.N.Y. 1978).

Accordingly, in the case at hand the court must determine whether, given the facts of this particular case, certification pursuant to Section 1292(b) is appropriate. First, the court must determine whether this case involves a controlling question of law as to which there is substantial ground for difference of opinion. Plaintiff asserts that the controlling question is "whether, in the context of a Rule 10b-5 open-market securities fraud litigation, a class action should be denied solely because the proposed representative may be subject to a defense of non-reliance and therefore could be considered an 'atypical' member of the class." While plaintiff has identified a controlling question of law, the court is of the opinion that there is not substantial ground for difference of opinion as to this question. Plaintiff has cited

no decisions by our Court of Appeals or by this court rejecting the *Greenspan* holding. Indeed, *Greenspan* is supported by substantial precedent. As discussed above, neither *Korn* v. *Franchard, supra,* nor *Green* v. *Wolf, supra,* is inconsistent with the court's *Greenspan holding*. Moreover, the court's holding in *Greenspan* and in the case at hand is fully consistent with the Supreme Court's opinion in *Eisen* v. *Carlisle & Jacquelin*. Finally, plaintiff's attempt to suggest a conflict between *Greenspan* and the decisions of the Third Circuit is untenable, in light of the Third Circuit's holding in *Zenith Laboratories, Inc.* v. *Carter-Wallace, Inc., supra* ("Since these unique defenses could conceivably become the focus of the entire litigation and divert much of [plaintiff's] attention from the suit as a whole, the remaining members of the class could be severely disadvantaged by [plaintiff's] representation.").

Second, the court must determine whether an immediate appeal may materially advance the ultimate termination of the litigation. As discussed above, certification is proper only under the most unusual circumstances where the immediate appeal might avoid protracted and costly litigation. Plaintiff has not shown any such unusual circumstances. While plaintiff may be forced to abandon this case because of the relatively small amount of plaintiff's individual claim, this case does not present unusual circumstances or an exceptional case in the context of securities class litigation. Plaintiff suggests that, if there is a reversal of this court's denial of class certification, issues may be resolved which are relevant to all class members. Again, this possibility hardly constitutes unusual circumstances where the immediate appeal might avoid protracted and costly litigation.

In summary, the court is of the opinion that plaintiff has not demonstrated a controlling question of law as to which

there is substantial ground for difference of opinion, nor has plaintiff demonstrated that an immediate appeal may materially advance the ultimate termination of the litigation. Accordingly, plaintiff's request for certification pursuant to 28 U.S.C. § 1292(b) must be denied.

Renewed Motions for Summary Judgment

Defendants have renewed their motions for an order, pursuant to Rule 56 of the Federal Rules of Civil Procedure, granting summary judgment in favor of defendants. These motions are renewed in light of the Supplemental Affidavit of Michael A. Blum, the broker through whom plaintiff purchased her shares of Allied Artists Industries, Inc. ("Allied").

In its memorandum opinion of January 16, 1980, the court reviewed the applicable law and noted that the presumption of reliance in a Section 10(b) action can be rebutted "with proof that the market's integrity and the alleged misrepresentations were not material to plaintiffs *or* that they relied primarily on another source." *Greenspan* v. *Brassier, supra,* 78 F.R.D. at 133 [emphasis added].[1] The court found in its memorandum opinion that there was a genuine issue as to whether the market's integrity and the alleged misrepresentations were material to plaintiff and whether plaintiff relied primarily on another source.

In particular, the court found that plaintiff's inquiry to her broker, asking if he had heard any negative news about

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[1] Plaintiff notes that the formulation of the methods of rebutting the presumption of reliance articulated by Judge MacMahon in *Greenspan* appears to differ somewhat from the formulation of the Ninth Circuit in *Blackie* v. *Barrack,* 524 F.2d 891 (9th Cir. 1975), *cert. denied,* 429 U.S. 816 (1976). Of course, the court now recognizes that the choice between the two formulations presents a close question. However, under principles of stare decisis, the court must follow the formulation it previously adopted in *Greenspan.*

Allied, might suggest that the market's integrity was material to plaintiff. Nothing in the Supplemental Affidavit of Michael A. Blum alters the court's evaluation of this issue.

Under this court's rule of law, as articulated in *Greenspan* v. *Brassler,* however, defendants may also rebut the presumption of reliance with proof that plaintiff relied primarily on another source. In its January 16, 1980, memorandum opinion, the court noted:

> [I]n her "corrected" deposition testimony, plaintiff stated that she bought Allied stock because of the newspaper article *and* her discussion with her broker concerning the Standard and Poor's "tear sheet." This "tear sheet" included financial information concerning Allied which had appeared in the 1978 Annual Report. Given plaintiff's "corrected" deposition testimony, there is a genuine issue as to whether plaintiff relied *primarily* on the newspaper article rather than the market's integrity or the alleged misrepresentations.

Panzirer v. *Wolf,* 79 Civ. 3445, slip op. at 9 (S.D.N.Y. Jan 16, 1980) [emphasis in original].

The Supplemental Affidavit of Michael A. Blum alters the court's analysis of the situation. Blum's Supplemental Affidavit makes clear that while he did discuss the "tear sheet" with plaintiff, he did not discuss the "tear sheet's" financial information:

> I did not discuss the financial statements or condition of Allied Artists with her, and have never read, either to myself or to Mrs. Panzirer, the financial information regarding Allied Artists which is contained in the tear sheet. I did not discuss Allied's price in relation to its financial condition. I do not

> remember any discussion as to whether there was negative news about Allied.

Moreover, the Supplemental Affidavit makes clear that Blum's discussion with plaintiff concerned primarily, if not exclusively, Allied's video cassette business:

> In my telephone conversation with Mrs. Panzirer, I read to her from the front side of the Standard & Poor's tear sheet, particularly that portion of the tear sheet relating to the video cassette business. A copy of the tear sheet is attached to the December 18, 1979 affidavit. We discussed the video cassette business and the Wall Street Journal article on that business. I suggested that the recent activity in the stock was probably due to speculation over that business. I told her that I did not follow the movie business because of its volatility and that E. F. Hutton & Co. did not follow Allied Artists.

Thus, the Supplemental Affidavit of Michael A. Blum, when read in conjunction with the rest of the record, establishes that plaintiff relied primarily on another source, rather than the market's integrity or the alleged misrepresentations. Plaintiff relied on a newspaper article concerning Allied's video cassette business and a discussion with her broker, also concerning Allied's video cassette business. Neither plaintiff nor her broker had read the 1978 Annual Report; moreover, neither plaintiff nor her broker had read the "tear sheet's" financial information regarding Allied. While plaintiff relied, in part, upon a discussion with her broker, this discussion did not concern Allied's financial statements or condition. Thus, there is no genuine issue as whether plaintiff relied primarily on another source; the

record shows that the presumption of reliance has been rebutted.

Plaintiff has attempted to create a genuine issue of material fact by submitting an affidavit in opposition to defendants' motions. Incredible as it may seem, plaintiff's affidavit contradicts *both* plaintiff's original deposition testimony *and* plaintiff's "corrected" deposition testimony. Thus, plaintiff has now given three *different* versions of the facts.

The Second Circuit has held that no *genuine* issue of fact is raised when a party attempts to create her own issue of fact by affidavit contradicting her prior testimony. *See Radobenko* v. *Automated Equipment Corp.*, 520 F.2d 540, 544 (9th Cir. 1975). "If a party who has been examined at length on deposition could raise an issue of fact simply by submitting an affidavit contradicting his own prior testimony, this would greatly diminish the utility of summary judgment as a procedure for screening out sham issues of fact." *Perma Research & Development Co.* v. *Singer Co.*, 410 F.2d 572, 578 (2d Cir. 1969); *accord, Bryant* v. *Western Electric Co.*, 572 F.2d 1087, 1088 (5th Cir. 1978) ("It is apparent that the testimony which the plaintiff gave before the summary judgment motion was filed provides the more reliable guide to the truth . . . .").

In her affidavit, plaintiff's latest version of the facts is that her conversation with Blum "was not limited to the video-cassette business of Allied but included some discussion of Allied's earnings and stock price information, and Allied's supposedly improving financial position." Plaintiff's affidavit directly contradicts her deposition testimony, both original and "corrected," in which she repeatedly stated that she did not remember anything concerning earnings or stock price information in her conversation with Blum. The court gives absolutely no credibility

to plaintiff's version of the facts in her affidavit, which is suddenly "recalled" after two contradictory versions in her deposition testimony. Not only does the affidavit fail to raise a genuine issue of material fact, but also plaintiff's frequent changes in her testimony show that she would have been unqualified to represent her class pursuant to Rule 23(a)(4).

Plaintiff has also attempted to create a genuine issue of material fact by submitting the affidavit of Leo E. Panzirer, plaintiff's husband. In his affidavit, Leo Panzirer tells of a conversation in which Blum advised him that, during the telephone conversation between Blum and plaintiff, Blum had reviewed Allied's earnings and stock price information with plaintiff. Under other circumstances, Leo Panzirer's affidavit might suffice to create a genuine issue. But in the case at hand, it should be noted that the telephone conversation at issue involved only Blum and plaintiff. Blum, in his Supplemental Affidavit, and plaintiff, in her original and "corrected" deposition testimony, both denied any discussion of earnings and stock price information. In light of the rather unusual circumstances of this case, Leo Panzirer's testimony will not suffice to to create a genuine issue of material fact.

In summary, there is no genuine issue as to the material fact that plaintiff relied primarily on another source, rather than the market's integrity and the alleged misrepresentation. Under the rule of law set forth by the court in *Greenspan* v. *Brassler,* defendants' renewed motions for summary judgment must be granted.

Motion for Leave to Intervene

Proposed intervenor Paul Block has moved for an order, pursuant to Rule 24 of the Federal Rules of Civil Pro-

cedure, granting Block leave to intervene and to serve and file his proposed intervenor's complaint. Rule 24(b) of the Federal Rules of Civil Procedure provides for permissive intervention.

> (2) when an applicant's claim or defense and the main action have a question of law or fact in common. . . . In exercising its discretion the court shall consider whether the intervention will unduly delay or prejudice the adjudication of the rights of the original parties.

In the case at hand, Block's claim is similar to, or almost identical with, that which was asserted by plaintiff in the main action. While none of the original parties press for denial of the intervention motion, the court is of the opinion that intervention should not be permitted pursuant to Rule 24(b). As the court explained in *Washington* v. *Wyman*, 54 F.R.D. 266, 272 (S.D.N.Y. 1971), "the intervenors cannot possibly have a claim or defense in common with a plaintiff who never had a claim." *Accord, Greer* v. *Blum*, 462 F. Supp. 619, 625 (S.D.N.Y. 1978); *Turner* v. *First Wisconsin Mortgage Trust*, 454 F. Supp. 899, 913 (E.D. Wis. 1978); *see Andujar* v. *Weinberger*, 69 F.R.D. 690, 697 (S.D.N.Y. 1976). As the Ninth Circuit has noted, "where the original plaintiffs were never qualified to represent the class, a motion to intervene represents a backdoor attempt to begin the action anew, and need not be granted." *Lidie* v. *California*, 478 F.2d 552, 555 (9th Cir. 1973). *But see Pikor* v. *Cinerama Productions Corp.*, 25 F.R.D. 92, 95 (S.D.N.Y. 1960) (stockholders' derivative suit); *Truncale* v. *Universal Pictures Co.*, 76 F. Supp. 465, 471 (S.D.N.Y. 1948).

In the case at hand, the court is of the opinion that the motion for leave to intervene should be denied, in light of the granting of summary judgment in favor of defendants in the main action.

Conclusion

For the reasons stated above, the court concludes that: 1) plaintiff's motion for reargument must be denied; 2) plaintiff's motion for certification pursuant to 28 U.S.C. § 1292(b) must be denied; 3) defendants' motions for summary judgment must be granted; and 4) proposed intervenor Block's motion to intervene should be denied.

Dated: New York, New York
April 21, 1980

SO ORDERED.

/s/ .....
CONSTANCE BAKER MOTLEY
U. S. D. J.

Order of the District Court (Motley, J.)
Dated April 21, 1980

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

79 Civ. 3445

ZELDA L. PANZIRER,

Plaintiff,

—against—

EMANUEL L. WOLF, JAY N. FELDMAN, C. RAY HOLLOWAY, WILLIAM V. LURIE, CARL PRAGER, JULIO PROIETTO, JACK M. SATTINGER and PRICE WATERHOUSE & CO.,

Defendants.

In accordance with the court's opinion of this date, it is hereby

ORDERED that plaintiff's motion, pursuant to Rule 9(g) of the General Rules of this Court, for leave to reargue plaintiff's motion for class action certification is denied; it is further

ORDERED that plaintiff's motion, pursuant to 28 U.S.C. § 2192(b), for certification of the issue of class adjudication to the Court of Appeals is denied; it is further

ORDERED that defendants' motions for an order, pursuant to Rule 56 of the Federal Rules of Civil Procedure, granting summary judgment in favor of defendants is granted; it is further

ORDERED that proposed intervenor Paul Block's motion for an order, pursuant to Rule 24 of the Federal Rules of

Order of District Court—April 21, 1980

Civil Procedure, granting Paul Block leave to intervene and to serve and file his proposed intervenor's complaint is denied.

Dated: New York, New York
April 21, 1980

SO ORDERED.

/s/ CONSTANCE BAKER MOTLEY
U.S.D.J.

Opinion of the District Court (Motley, J.)
Dated January 16, 1980

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

79 Civ. 3445

ZELDA L. PANZIRER,

Plaintiff,

—against—

EMANUEL L. WOLF, JAY N. FELDMAN, C. RAY HOLLOWAY, WILLIAM V. LURIE, CARL PRAGER, JULIO PROIETTO, JACK M. SATTINGER and PRICE WATERHOUSE & CO.,

Defendants.

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Opinion of District Court—January 16, 1980

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CONSTANCE BAKER MOTLEY, D. J.

MEMORANDUM OPINION

Defendants have moved for an order, pursuant to Rule 56 of the Federal Rules of Civil Procedure, granting summary judgment in favor of defendants and dismissing the amended complaint. Plaintiff has also moved for an order, pursuant to Rule 23 of the Federal Rules of Civil Procedure, determining that plaintiff may maintain this action as a class action on behalf of all purchasers of Allied Artists Industries, Inc. ("Allied") common stock between August 18, 1978, and April 4, 1979.

The amended complaint in this action alleges a violation of Section 10(b) of the Securities Exchange Act of 1934, as amended, 15 U.S.C. § 78j(b), and Rule 10b-5 of the Securities and Exchange Commission's rules and regulations promulgated thereunder, 17 C.F.R. § 240.10b-5. The amended complaint in this action alleges that defendants caused Allied to issue to the investing public false and misleading statements about Allied's financial condition. The allegations relate to Allied's 1978 Annual Report, which included financial statements for the fiscal year ending March 31, 1978.

Plaintiff alleges that in purchasing 500 shares of Allied stock on September 29, 1978, she "relied upon the aforesaid materially false and misleading statements of defendants

and/or upon the integrity of the market price of Allied's stock as reflected by the impact of said statements on the market for Allied securities." Plaintiff further alleges that these misrepresentations were part of a scheme to portray falsely Allied's financial condition and to cause Allied's stock to trade at artificially high prices.

On November 6, 1979, plaintiff's deposition was taken by defendants. Plaintiff testified that she was not aware of Allied's financial position at the time she purchased her Allied stock. Plaintiff testified that she did not see a copy of Allied's 1978 Annual Report prior to her purchase of Allied shares on September 28, 1978. In short, plaintiff received no financial information about Allied. Instead, plaintiff testified that she bought Allied stock because of a newspaper article appearing in the *Wall Street Journal* on the day of her purchase, September 29, 1978. Plaintiff testified that she telephoned her broker, who told her that there was no negative news about Allied. Plaintiff testified that other than the newspaper article and the discussion with her broker, she did not rely on any other information about Allied in making her purchase. With respect to the newspaper article, plaintiff testified:

> I never knew specifically what Allied Artists did. Of course, the name is known to me as being in the film business. I didn't know of any of their subsidiaries or what other business they were involved in. But this article was very interesting because this Mr. Racz gave a glowing report. He said, "Allied Artists, besides having a head start in videotapes and cassettes, is negotiating with the TV networks, other film producers and makers of educational films"—of course I am involved in educational films, as I am a teacher currently not that active, but we have used

> so many educational films—"to put their films on video cassettes."
>
> "The educational informational area constitutes a tremendous market for video cassettes, says Mr. Racz, adding: 'We continue to be bullish on Allied Artists. It's an attractive, turn-around situation.'" End of quote.

Panzirer dep. at 131-32.

On December 21, 1979, during oral argument before the court, plaintiff's attorney noted that defendants had not submitted plaintiff's deposition to her for examination and signing. It was then agreed that defendants would submit plaintiff's deposition to her sometime following the oral argument.

On January 3, 1980, plaintiff signed her deposition, after making numerous changes in her testimony. Accompanying her signed deposition, as changed, was plaintiff's affidavit which was submitted to explain the "corrections made in [her] deposition transcript prior to the execution thereof."

In her deposition testimony, as "corrected' on January 3, 1980, plaintiff states that her broker read to her from the Standard and Poor's "tear sheet" during their telephone conversation of September 29, 1978. Plaintiff states in her "corrected" deposition testimony that at the time of purchase she knew only what she read in the newspaper article *and* what her broker told her over the phone. Thus, in her "corrected" deposition testimony, plaintiff states that "[a]side from what [she] testified earlier," she wasn't aware of Allied's financial position at the time she purchased and that "[a]side from what she testified earlier," she received no financial information about Allied from her broker. In short, plaintiff now testifies that she bought Allied stock because of the newspaper article and her discussion with her broker.

Plaintiff's Deposition Testimony

Plaintiff's "corrections" in her deposition testimony, while shockingly drastic, nonetheless complied with the requirements of Rule 30(e) of the Federal Rules of Civil Procedure. Rule 30(e) provides:

> When the testimony is fully transcribed the deposition shall be submitted to the witness for examination and shall be read to or by him, unless such examination and reading are waived by the witness and by the parties. Any changes in form or substance which the witness desires to make shall be entered upon the deposition by the officer with a statement of the reasons given by the witness for making them. The deposition shall then be signed by the witness, unless the parties by stipulation waive the signing or the witness is ill or cannot be found or refuses to sign.

This court has previously held that Rule 30(e) places no limitations on the type of changes that may be made by a witness before signing his deposition. *Allen & Co.* v. *Occidental Petroleum Corp.*, 49 F.R.D. 337, 340 (S.D.N.Y. 1970). The witness may make changes of any nature, no matter how fundamental or substantial. *Id.*

Defendants argue that, Rule 30(e) notwithstanding, "[p]laintiff's belated contradictions of her prior deposition testimony cannot create a genuine issue of fact to affect a motion for summary judgment." *See, e.g., Bryant* v. *Western Electric Co.*, 572 F.2d 1087, 1088 (5th Cir. 1978); *Radobenko* v. *Automated Equipment Corp.*, 520 F.2d 540, 543-44 (9th Cir. 1975); *Perma Research and Development Co.* v. *Singer Co.*, 410 F.2d 572, 578 (2d Cir. 1969). The

court recognizes, of course, that plaintiff's "corrections" in her deposition testimony are suspicious, to say the least, especially in light of the fact that the numerous changes were made following the footsteps of defendants' motion for summary judgment. Nevertheless, the changes were made within the restrictions of Rule 30(e), and any issues of plaintiff's credibility in making the changes must be resolved by the jury at trial. While the authorities cited by defendants suggest that a party may not defeat a summary judgment motion by contradicting prior deposition testimony with a subsequent affidavit, these authorities cannot be read as precluding a party from changing deposition testimony prior to signature.

Reliance

The critical issue posed by defendants' motion for summary judgment is whether there are any genuine issues as to any material facts concerning plaintiff's reliance. Of course, in a case involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery. *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 153 (1972). "All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision." *Id.* at 153-54. In other words, in a case involving primarily a failure to disclose, there is a presumption of reasonable reliance in order to avoid an overly difficult burden of proof. *Chris-Craft Industries, Inc.* v. *Piper Aircraft Corp.*, 480 F.2d 341, 374 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973). This presumption of reliance, however, may be rebutted by defendants, at least under Second Circuit law. *See Titan Group, Inc.* v. *Faggen*, 513 F.2d 234, 239 (2d Cir.), *cert. denied*, 423 U.S. 840 (1975); Note, *The Reli-*

ance Requirement in Private Actions under SEC Rule 10b-5, 88 Harv. L. Rev. 584, 600 n.75 (1975). *But see Chris-Craft Industries, Inc.* v. *Piper Aircraft Corp., supra*, 480 F.2d at 399-400 (Mansfield, J., concurring & dissenting).

In the case at hand, any presumption that plaintiff relied upon the alleged misrepresentations or omissions in Allied's 1978 Annual Report have been rebutted by plaintiff's own statements in her deposition testimony, even as "corrected." Plaintiff testified that she did not see a copy of Allied's 1978 Annual Report prior to her purchase of Allied shares. Plaintiff's testimony would seem to rebut any presumption that plaintiff relied upon misrepresentations or omissions in Allied's 1978 Annual Report. *See Vervaeck* v. *Chiles, Heider & Co.*, 578 F.2d 713, 718-19 (8th Cir. 1978); *Tanzer* v. *Sharon Steel Corp.*, [1979 Transfer Binder] Fed. Sec. L. Rep. ¶ 96,915, at 95,796 (S.D.N.Y. June 22, 1979).

Plaintiff also asserts, however, a "fraud on the market" theory—that is, a theory that plaintiff relied upon the integrity of the market price of Allied's stock, a price reflecting the impact of the allegedly false and misleading statements on the market for Allied securities. In a Section 10(b) action, reliance is presumed once it is established that a material misrepresentation affected the price of stock traded on the open market. *Ross* v. *A.H. Robins Co.*, [Current] Fed. Sec. L. Rep. ¶ 97,115 (2d Cir. Sept. 24, 1979). This presumption of reliance can be rebutted "with proof that the market's integrity and the alleged misrepresentations were not material to plaintiffs or that they relied primarily on another source." *Greenspan* v. *Brassler*, 78 F.R.D. 130, 133 (S.D.N.Y. 1978).

In the case at hand, there is a genuine issue as to whether the market's integrity and the alleged misrepresentations

were material to plaintiff and whether plaintiff relied primarily on another source. In her deposition testimony, plaintiff stated that she asked her broker if he had heard any negative news about Allied. After the broker told plaintiff that there was no negative news about Allied, plaintiff purchased Allied stock. Plaintiff's inquiry to her broker might suggest that the market's integrity *was* material to plaintiff. Moreover, in her "corrected" deposition testimony, plaintiff stated that she bought Allied stock because of the newspaper article *and* her discussion with her broker concerning the Standard and Poor's "tear sheet." This "tear sheet" included financial information concerning Allied which had appeared in the 1978 Annual Report. Given plaintiff's "corrected" deposition testimony, there is a genuine issue as to whether plaintiff relied *primarily* on the newspaper article rather than the market's integrity or the alleged misrepresentations. As recognized above, this court has serious reservations regarding the credibility of plaintiff's changes in her deposition testimony. Nevertheless, these issues are best resolved by the jury at trial. In light of the genuine issue as to plaintiff's reliance, a material fact in this action, defendants' motion for summary judgment must be denied.

Class Action

Plaintiff has also moved for an order, pursuant to Rule 23 of the Federal Rules of Civil Procedure, determining that plaintiff may maintain this action as a class action. Certification of this suit as a class action is dependent on plaintiff's proof that each of the requirements of Rule 23(a) has been met. The court concludes that plaintiff does not meet the requirement of Rule 23(a)(3), and accordingly, plaintiff's motion is denied without reaching the question whether plaintiff has met the requirements of Rules 23(a)(1), 23(a)(2), 23(a)(3), or 23(b)(3).

Rule 23(a)(3) provides that a prerequisite to a class action is that "the claims or defenses of the representative parties are typical of the claims or defenses of the class." In the case at hand, the record before the court clearly indicates that plaintiff may be subject to defenses not applicable to other class members. Plaintiff's possible reliance on a newspaper article relating to Allied's video cassette business, rather than on the market's integrity or the alleged misrepresentations in the 1978 Annual Report, raises issues qualitatively different from the questions of individual reliance normally inherent in a fraud on the market suit. Thus, certification of this suit as a class action must be denied since plaintiff is subject to unique defenses that will unnecessarily prejudice the class's probability of success. Although the evidence is insufficient to compel summary judgment in defendants' favor, plaintiff may be subject to the defenses that 1) she relied primarily on a source other than the market's integrity and the alleged misrepresentation or 2) that the market's integrity and the alleged misrepresentation were not directly material to plaintiff.

In this respect, the court's denial of plaintiff's motion for class certification is directly controlled by this court's holding in *Greenspan* v. *Brassler, supra.* In *Greenspan,* a "fraud on the market" case, the court found that factual issues concerning reliance and materiality precluded granting defendants' motion for summary judgment. There was evidence in *Greenspan* that plaintiffs' purchases were made in reliance on the recommendation of a plaintiff's brother, rather than on plaintiff's analysis of the market performance of the stock. In language directly applicable to the case at hand, the court held:

> [A]lthough the evidence is insufficient to compel summary judgment in defendants' favor, it does indicate that plaintiffs may be subject to defenses not appli-

cable to other class members. Plaintiffs' third purchase and their possible reliance on Noah's recommendation raise issues qualitatively different from the questions of individual reliance inherent in a fraud on the market suit. *See, e.g., Green* v. *Wolf Corp.*, 406 F.2d 291 (2d Cir. 1968), *cert. denied*, 395 U.S. 977, 89 S.Ct. 2131, 23 L.Ed.2d 766 (1969); *Mersay* v. *First Republic Corp.*, 43 F.R.D. 465 (S.D.N.Y. 1968). Although those questions normally do not preclude certification, class status must be denied when, as here, the putative representative is subject to unique defenses that will unnecessarily prejudice the class's probability of success. *Koos* v. *First Nat'l Bank*, 496 F.2d 1162 (7th Cir. 1974); *Kraus* v. *Paterson Parchment Paper Co.*, 65 F.R.D. 368 (S.D.N.Y. 1974). But see *Dorfman* v. *First Boston Corp.*, 62 F.R.D. 466 (E.D.Pa. 1974).

78 F.R.D. 132. Applying this courts' standards as set forth in *Greenspan*, in the case at hand plaintiff's motion for class certification must be denied.

Conclusion

For the reasons stated above, defendants' motion for summary judgment is denied, and plaintiff's motion for class certification is also denied.

Dated: New York, New York
January 16, 1980

SO ORDERED.

/s/ .....
CONSTANCE BAKER MOTLEY
U. S. D. J.

Order of the District Court (Motley, J.)
Dated January 16, 1980

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

79 Civ. 3445

ZELDA L. PANZIRER,

Plaintiff,

—against—

EMANUEL L. WOLF, JAY N. FELDMAN, C. RAY HOLLOWAY, WILLIAM V. LURIE, CARL PRAGER, JULIO PROIETTO, JACK M. SATTINGER and PRICE WATERHOUSE & CO.,

Defendants.

In accordance with the court's memorandum opinion of this date, it is hereby

ORDERED that defendants' motions for summary judgment are denied; and it is further

ORDERED that plaintiff's motion for class certification is denied.

Dated: New York, New York
January 16, 1980

SO ORDERED.

/s/ CONSTANCE BAKER MOTLEY
U. S. D. J.

Marcial, *Prospects for New Home Video Equipment Spark Analyst Optimism About the Industry,*
The Wall Street Journal,
September 29, 1978, at 47, col. 3

Prospects for New Home-Video Equipment Spark Analyst Optimism About the Industry

By Gene G. Marcial

First there was radio, then came television. Will the video tape-disc player and recorder be the next dominant form of home entertainment?

Some Wall Street analysts think so, and they're talking bullishly about companies that are beginning to participate in what they expect will be an important market in the 1980s.

Home screening systems, involving products such as video cartridge-cassette recorders . . . and home-video camera and video-disc players, will be "an important prestige leisure-time entertainment" of the 1980s, says David Londoner, vice president at Wertheim & Co.

Heard on the Street

Theodore W. Anderson of Argus Research Corp. believes these video products will generate "vast changes in the consumer-oriented communications industry" in the next few years, which should favor certain consumer-electronic and entertainment companies. He expects unit sales of the video products to grow at "very rapid rates in the next five years—at least 20% annually and perhaps as much as 30%."

During the 1980s, many homes will have a "screening room" equipped with large television-type screens, video-disc players and video-tape recorders, says Wertheim's Mr. Londoner. Thus, a family's next "prestige spending" will be for these types of home entertainment, he adds.

Analysts say that part of the disappointment with network television today is the viewer's lack of control over the timing and availability of programs. Part of this problem, they say, will be alleviated by the video-tape recorders and video-disc players. A video recorder is a device that copies the picture sound signals received on a television set and stores them on a recording medium, either on tape or disc.

Video cartridge recorders (VCR) such as RCA's VCT-400, allow the user to tape automatically with a timing device. They also are able to play preprogrammed material, such as movies, which can be obtained from some suppliers, such as Twentieth Century-Fox, Allied Artists, Avco Embassy, and Magnetic Video.

Several analysts contend that Allied Artists is in a good position to take advantage of the growing demand for video tapes, having pioneered the development of prerecorded cassettes.

Andrew G. Racz, of Philips, Appel & Walden Inc., says Allied Artists, besides having a head start in video tapes and cassettes, is negotiating with TV networks other film producers and makers of educational films to put their films on video cassettes. "The educational and informational area constitutes a tremendous market for video cassettes," says Mr. Racz, adding: "We continue to be bullish on Allied Artists. It's an attractive, turnaround situation."

Argus's Mr. Anderson recommends RCA and Matsushita Electric for longer-term participation in the infant VCR industry. The two are leading marketers in the U.S. of VCR players and accessories.

Mr. Anderson says RCA, "with a mix of defensive, steady growth consumer-service businesses and strong consumer and industrial electronics divisions," is rated a buy. But Matsushita, "an attractive company in most respects," is rated a near-term hold because of the yen's sharp rise against the dollar, which, he expects, will hurt earnings during the next few months.

Matsushita produces the most automated VCR and color-TV sets in Japan and probably in the world, says Mr. Anderson, and is the leading supplier to other companies, including RCA, of VCRs and accessories.

Mr. Anderson expects growth of the VCR market to expand rapidly. "This prospect reflects greater consumer awareness, stepped-up advertising by marketers, such as RCA, and improved technology," he says. An accepted industry forecast, he adds, is that 500,000 units will be sold this year, one million in 1978 and 1.5 million in 1980.

Mr. Anderson rates Zenith, U.S. marketer of Sony's Betamax video recorders, a "weak hold." Betamax lacks some of the important features of RCA's Selectavision 400, Mr. Anderson contends.

Wertheim's Mr. Londoner believes the video-disc devices are a more inexpensive means of delivering entertainment inside homes that are of "excellent quality." Video discs are basically similar to phonograph records. You can't record on them, however, as with a tape.

Mr. Londoner says MCA and North American Philips will introduce video-disc devices this December on a regional basis. MCA will make discs and North American will produce disc players. MCA and Pioneer Electronics of Japan have formed a joint venture to manufacture disc players, initially for commercial users, such as industrial companies. They are expected to produce consumer video-disc players sometime in 1980, Mr. Londoner says.

He expects other companies, such as Disney, Zenith, Sony and Hitachi soon will enter the disc market. He says MCA and Disney are on Wertheim's purchase list, but that any company with a quality film library and continuing film production should benefit from developments in video home entertainment.

Opposition

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No. 81-1998

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

PRICE WATERHOUSE,

Petitioner,

-v.-

ZELDA L. PANZIRER,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF RESPONDENT ZELDA PANZIRER IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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MISCELLANEOUS

"The Fraud on The Market Theory", 92 Harv. L. Rev. 1143 (1982) 5, 6

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NO. 81-1998

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

PRICE WATERHOUSE,

Plaintiff,

vs.

ZELDA L. PANZIRER,

Respondent.

BRIEF OF RESPONDENT ZELDA PANZIRER IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

INTRODUCTION

Respondent Zelda L. Panzirer[1] respectfully submits this brief in opposition to the petition of Price Waterhouse for a writ of certiorari to the United States Court of Appeals for the Second Circuit.[2]

Petitioner seeks review of the decision by the Court of Appeals for the Second Circuit which found that summary judgment had been improvidently granted by the District Court. Price Waterhouse seeks to establish a question for review unrelated to

1. Mrs. Panzirer has also petitioned for a writ of certiorari (No. 81-2011) to seek review of the decision of the Court of Appeals affirming the District Court's denial of class certification on the grounds that personal characteristics of the plaintiff not germane to the issues in the case rendered her an inadequate class representative under Rule 23(a)(4).

2. Petitioner Price Waterhouse takes the position that the individual defendants "have no personal interest in the outcome of this petition for certiorari." They are wrong. The individual defendants filed a brief in support of the petition in which they state that the Court of Appeals' opinion applied equally to them.

the issues before the courts below and misleading at its core. Price Waterhouse ignores the facts as found by the Court of Appeals and presents its own version unsupported by the record and at variance with the two other versions of the "facts" it presented to the lower courts.

FACTS OF RECORD

The facts, as found by the Court of Appeals, differ markedly from those presented by Price Waterhouse.

Mrs. Panzirer's Stock Purchases

In September 1978, Allied Artists Industries, Inc. ("Allied") issued its 1978 Annual Report showing a profit for the year and which respondent contends is fraudulently false and misleading with regard to Allied's financial condition and prospects. Thereafter, on September 28, 1978, she purchased shares of Allied common stock (the "Shares"), after reading an article in *The Wall Street Journal* recommending Allied as a "turnaround" situation and stating that it was a "good position to take advantage of growing demand for video tapes," particularly educational products.

Mrs. Panzirer had been a substitute school teacher. The item on the educational use of the video cassettes caught her eye. She checked the price of Allied common stock which was listed on the American Stock Exchange and had traded at between $5 and $6 1/2 on September 28th. Respondent called her broker, Michael Blum, of E.F. Hutton. She asked if there was any negative news about Allied. Mr. Blum said that neither he nor E.F. Hutton followed the company, but after several minutes delay and a glance at Standard & Poor's tear sheet on Allied, he reported that there was no negative news. Mrs. Panzirer ordered 200 Shares. Later, after discussing the purchase with her husband, she phoned Mr. Blum a second time to increase her order to 500 Shares. E.F. Hutton purchased the Shares for Mrs. Panzirer at a September 29th market price of $7 per Share.

The Fraud

The Annual Report, issued on September 8, 1978, allegedly contained numerous misrepresentations and omissions. The principal alleged misrepresentations was the report of profits for that year based in part on full receipts from Allied's film, "The Betsy". In fact, Allied was required to split those receipts with the film's overseas distributor, United Artists and thus lost money in 1978.

The principal alleged omission was the failure of the Annual Report to include a qualification by Allied's accountants stating their doubts as to Allied's ability to function as a going concern. Originally Price Waterhouse had qualified their opinion but withdrew their qualification under pressure prior to the publication of the annual report.[3]

Allied's Shares closed at $2 7/8 per Share on the day the Annual Report was issued. It rose precepitously in the next few weeks and peaked at $7 3/8 per Share on October 2, 1978.

Six months later Allied was bankrupt; the Shares are worthless today.

In her complaint, Mrs. Panzirer alleged that in making her purchase she relied on the "integrity of the market" for Allied's Shares. She asserts that the Annual Report affected the market and, therefore, she relied on the Report through her reliance on the integrity of the market.

THE DISTORTION OF THE OPINIONS BY PETITIONER

Price Waterhouse's petition obscures the rulings of both the District Court and the Court of Appeals. It has presented three different versions of the facts to those different courts.

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3. The Price Waterhouse statement that its opinion was qualified is a half truth. It was qualified but, not as to the key factor: "going concern status". That qualification had been removed by the auditors before publications of the Annual Report.

The District Court granted summary judgment because it found, at defendants urging, that Mrs. Panzirer had relied *primarily* upon a source other than the integrity of the market and Allied's financial condition in making her purchase:

> "Moreover, the Supplemental Affidavit makes clear that Mr. Blum's discussion with plaintiff concerned *primarily*, if not exclusively, Allied's video cassette business ... when read in conjunction with the rest of the record, it establishes that plaintiff relied *primarily* on another source, rather than the market's integrity or the alleged misrepresentation." (Emphasis added)

The District Court, thus, contrary to Petitioner's urging here, never even considered the fraud on the market theory because Price Waterhouse never even questioned it.

The Opinion of the Court of Appeals

The Court of Appeals reversed the District Court's grant of summary judgment, finding no support in the law for a test of reliance which weighs the importance of the factors considered in making a purchase.

The Court of Appeals concluded from the record that Mrs. Panzirer's purchase of Allied Shares was caused by her perusal of *The Wall Street Journal* column. Her knowledge of the price of the stock and her conversation with her broker, according to the Court of Appeals, were neutral factors that presented no impediment to her acting on the favorable notice in *The Wall Street Journal*. The Court concluded that if Allied's reports had been accurate, the stock analysts interviewed by the *Journal* would not have mentioned the company favorably, the *Journal* would not have devoted two paragraphs to Allied's prospects and Mrs. Panzirer would not have been led by the article to buy her stock.

The Argument of Price Waterhouse

Abandoning the position it took below, Petitioner now disputes the factual conclusions of both the District Court and the Court of Appeals, ignores the record, and states, without any support,

that Mrs. Panzirer's *only interest* (not "primary") was in video cassettes, divorced, totally from the company's financial condition.

Price Waterhouse then argues that its fraud could not affect video cassettes and, in any event, it had no duty to purchasers of Shares to tell the truth. Finally, Price Waterhouse, constructs a house of horribles outside the world of real life decisions concerning investments, rejected by each Court of Appeals which has considered the issue.

The record is clear. Mrs. Panzirer's was attracted to Allied[4] by an analysis appearing in *The Wall Street Journal's* daily column "Heard on the Street". The article quoting a respected securities analyst stated:

> --"Allied Artists is in a *good position* to take advantage of the growing demand for video types...."
>
> --"We continue to be *bullish* on Allied Artists."
>
> --"It's an attractive *turnaround* situation."
> (Emphasis added)

The words "turnaround", "good position" and "bullish" have only one meaning in the world of stock investment. They refer to an analysis of financial conditions and the market's response thereto. Insolvent companies with no assets and no prospects are not promoted as good "turnaround" prospects by respected analysts.

ARGUMENT

FRAUD ON THE MARKET CLAIMS HAVE BEEN ACCEPTED BY EACH COURT OF APPEALS WHICH HAVE CONSIDERED THEM[5]

Courts which have considered the issue determined by the Second Circuit, a claim for relief under the securities laws arising

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4. Allied was in an industry in which Mrs. Panzirer was interested Selecting a stock within an industry is a common method of investment selection.

5. We acknowledge our reliance on a note at 92 Harvard Law Review 1143 (1982) "*The Fraud on the Market Theory* for much of our argument.

from a fraud on the market, have all determined the issue in the same way. We know of no decision of any Court of Appeals contrary to the decision of the Second Circuit.

The fraud on the market theory has been accepted by the Second, Fifth and Ninth Circuits. *Panzirer* v. *Wolf*, 663 F.2d 365 (2d Cir. 1981); *Shores* v. *Sklar*, 647 F.2d 462 (5th Cir. 1981) (en banc); *Blackie* v. *Barrack*, 524 F.2d 891 (9th Cir. 1975), *cert. denied*, 429 U.S. 816 (1976).

These decisions rest in part upon the Supreme Court's decision in *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972). Later opinions of district and circuit courts interpreted *Ute* as providing in non-disclosure cases that materiality establishes a presumption of reliance. *Ute's* holding both relieves the plaintiff of an onerous task of proof and strengthens the current force of private actions under Rule 10b-5. *See e.g.*, *Rifkin* v. *Crow*, 574 F.2d 256, 262 (5th Cir. 1978); *Holdsworth* v. *Strong*, 545 F.2d 687, 695 (9th Cir. 1976) (en banc), *cert. denied*, 430 U.S. 955 (1977); *Chelsea Associates* v. *Rapanos*, 527 F.2d 1266, 1271 (6th Cir. 1975); *Carras* v. *Burns*, 516 F.2d 251, 257 (4th cir. 1975); *Blackie* v. *Barrack*, 524 F.2d 891, 908 (9th Cir. 1975).

The fraud on the market theory first termed the "artificial inflated market price theory" preceded *Ute*. *Green* v. *Wolf Corp.*, 406 F.2d 291 295 (2d Cir. 1968) *cert. denied*, 395 U.S. 977 1969); *In re Memorex Securities Cases*, 61 F.R.D. 88, 100-01 (N.D. Calif. 1973); *see*, *Tucker* v. *Arthur Anderson & Co.*, 67 F.R.D. 468, 480-81 (S.D.N.Y. 1975); and the many cases cited in the Harvard Law Review note *supra*.

Consistent with *Panzirer* the Second Circuit applied the fraud on the market theory as early as 1973. In *Chris-Craft Industries* v. *Piper Aircraft Corp.*, 480 F.2d 341 (2d Cir.), *cert. denied* 414 U.S. 9, 10 (1973), the court speaking in terms of "constructive reliance" presumed reliance. 480 F.2d at 374; *Accord, In re U.S. Financial Securities Litiga-tion*, 69 F.R.D. 24, 44 (S.D. Calif. 1975).

Similarly in *Schlick* v. *Penn-Dixie Cement Corp.*, 570 F.2d 374 (2d Cir. 1974), *cert. denied* 421 U.S. 976 (1975), the court held,

that because a deceptive proxy statement was only one part of the broad scheme including market manipulation, plaintiff was not required to prove that he relied on the misstatements or omissions of the proxy materials in reaching his investment decision but that only that he was injured by the exchange ratio. 507 F.2d at 381.

Likewise, in *Ross* v. *A.H. Robins Co.*, 607 F.2d 545- (2d Cir. 1979), the Second Circuit said:

> "In a Section 10b action, however, reliance is presumed once the materiality of an omission is established, *Affiliated Ute Citizens* v. *U.S.*, *supra* 406 U.S. 128 (1972), or the material misrepresentation affected the market prices of the stock on the open market."

In re LTV Securities Litigation, 88 F.R.D. 134, (N.D. Tex., 1980) (Higginbotham, J.), the court explained most articulately the rationale underlying the presumption of reliance in an open market securities fraud class action.

> "With the presence of a market, the market is interposed between seller and buyer, and ideally, transmits information to the investor in the processed form of a market price. Thus, the market is performing a substantial part of the valuation process performed by the investor in a face-to-face transaction. The market is acting as an unpaid agent, informing him that given all the information available to it, the value of the stock is worth the market price. If the investor did not rely on such agent there is no reliance. Thus, a defendant should be able to attack such an investor's claim in much the same way he would face-toface transaction - being allowed to offer proof that the reliance was upon matters extraneous to the market (to render the presumption)". (*Id.* at 98,231).

In *Shores* v. *Sklar*, 47 F.2d 462 (5th Cir. 1981) (en banc), the court accepted the fraud on the market theory predicated in substantial part on *In re LTV SecuritiesLitigation*, 88 F.R.D. 134 (142) N.D. Tex. 1980) and *Sargent* v. *Genesco, Inc.*, 75 F.R.D. 79, 84 (M.D. Fla. 1977).

Although *Shores*, dealt with "new issues", the opinion in broader terms adopts the fraud on the market theory of *Blackie*,

A.H. Robins, LTV and *Panzirer*. Here, however, it is unnecesary for us to rely on *Shores* because it is undisputed that Allied Shares were traded in an active developed market on an exchange similar to the situations where fraud on the market has been accepted.

Petitioner also cites *Veraecke* v. *Chiles, Heider & Co.*, 578 F.2d 713 (8th Cir. 1978), which was not an omissions case. The Eighth Circuit ruled that in a misrepresentation case there was no presumption of reliance. After trial, the lower court had concluded that plaintiff had not relied directly or indirectly on the alleged misrepresentation. 578 F.2d at 719.

Finally, Petitioner presents a misreading of the Second Circuit's opinion in *Wilson* v. *Comtech Telecommunica-tions, Corp.*, 648 F.2d 88 (2d Cir. 1981). Indeed, *Wilson* was relied upon by the Second Circuit in its opinion here as supporting its ruling. The Second Circuit found no inconsistency between *Wilson* and *Panzirer*.

The court decided *Wilson* against plaintiff because there was no showing that plaintiff had purchased any shares of Comtech in reliance upon any misstatement of material fact. Instead, plaintiff's purchase there was based on a recommendation by his broker that he should take advantage of a *decline* in the price of the stock.

Blackie, *Panzirer* and most of the other cases recognize that fraud on the market claims arise in large and impersonal markets. Those markets respond to information published concerning companies whose securities are traded. In such a setting, the reliance of some traders upon a material deception influences market prices and, thereby, affects even traders who never read or hear of the deception.

Available and emperical evidence suggests that large impersonal markets to which the courts have applied the "efficient market theory" are indeed efficient. *See*, *R. Brealey* and *S. Meyers*, *Principals of Corporate Finance*, 260-265 (1981); *J.*

Loire and *M. Hamilton, The Stock Market: Theories in Evidence*, 96-97 (1973); *W. Sharpe, Investments*, 71-72 (2d Ed. 1981).

The opinions of the Court of Appeals for the Second Circuit, the Ninth Circuit, the Fifth Circuit and the lower court in *LTV*, are consistent with this realistic view.

It was the real world of investing that the Court of Appeals in *Blackie* discussed with regard to the issue of reliance in a fraud on the market case:

> "A purchaser on the stock exchanges may be either unaware of a specific false representation, or may not directly rely on it; he may purchase because of a favorable price trend, price earnings ratio, or some other factor. Nevertheless, he relies generally on the supposition that that *marketprice is validly set and that no unsuspected manipulation has artifically inflated the price, and thus indirectly on the truth of the representations underlying the stock price* -- whether he is aware of it or not, the price he pays reflects material misrepresentations. Requiring direct proof from each purchaser that he relied on a particular representation when purchasing would defeat recovery by those whose reliance was indirect, despite the fact the causational chain is broken only if the purchaser would have purchased the stock even had he known of the misrepresentation. We decline to leave such open market purchasers unprotected. *The statute and rule are designed to foster an expectation that securities markets are free from fraud -- an expectation on which purchasers should be able to rely*". *Id.*, 524 F.2d at 907 (Emphasis added.)

Ross v. *A.H. Robins Company*, *supra*, 607 F.2d 545; *In Re LTV Securities Litigation supra*, 88 F.R.D. 134 ; Note; "The Reliance Requirement in Private Actions Under SEC Rule 10b-5", 88 Harv.L.Rev. 584, 589 (1975).

What Price Waterhouse is attempting to do here is permit accountants to issue fraudulently false financial statements relied upon by the investment community in making recommendations to the public and upon which the public does rely. Petitioner

seeks to create a barrier around their false statements which could be scaled only where there exists direct communication between the accountants and the purchaser. Such a limited view of accountants liability does not comport with the realities of the securities market. Price Waterhouse seeks to revert to the years when privity of contract artificially barred the defrauded plaintiffs from recovering from accounting firms.

Petitioner seeks to avoid its liability to the purchasers of Allied shares by saying financial statements are not written to be relied on by the investing public. But, as to this issue all courts are in agreement: accountants liability extends beyond its clients to others who rely on that opinion directly or indirectly to their detriment. The facts in each case, including *Panzirer*, will determine the nature and extent of such reliance as well as the other issues of fact in the lawsuit.

Dated: New York, New York
May 26, 1982

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Supplemental Respondent's Brief

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No. 81-1998

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

PRICE WATERHOUSE,

Petitioner,

v.

ZELDA L. PANZIRER,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

RESPONDENT ZELDA PANZIRER'S SUGGESTION OF MOOTNESS

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IN THE

Supreme Court of the United States

October Term, 1981

No. 81-1998

PRICE WATERHOUSE,

Plaintiff,

v.

ZELDA L. PANZIRER,

Respondent.

RESPONDENT ZELDA L. PANZIRER'S SUGGESTION OF MOOTNESS

Respondent Zelda L. Panzirer respectfully submits this suggestion of mootness and seeks dismissal of this action as to which this Court has granted a writ of certiorari to the United States Court of Appeals for the Second Circuit.[1]

Respondent Panzirer, who is the plaintiff, has directed her attorneys not to proceed with the action and to dismiss it with prejudice against all defendants because she no longer has any substantial stake in the litigation.

Mrs. Panzirer brought this action as a class action. The United States District Court for the Southern District of New York denied plaintiff's motion to certify the action as a class

1. On July 13, 1982, Mrs. Panzirer, by letter of her attorneys, advised defendants of her position and offered to enter into a stipulation to dismiss the action with prejudice and to pay the taxable fees and costs that may be due. Petitioner declined to enter into such a stipulation. Only July 22, 1982, Respondent, by her counsel, wrote to the Clerk of this Court advising him of her determination not to proceed and requesting that the action be dismissed. The Clerk advised us that a formal suggestion of mootness was required.

action and granted defendants' motions for summary judgment. *Panzirer v. Wolf*, [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,251 (S.D.N.Y. January 16, 1980), and Fed. Sec. L. Rep. (CCH) ¶ 97,363 (S.D.N.Y. April 21, 1980). The Court of Appeals for the Second Circuit affirmed the denial of class certification but reversed the grant of summary judgment. *Panzirer v. Wolf*, 663 F.2d 365 (2d Cir. 1981). The Supreme Court denied plaintiff Panzirer's petition for a writ of certiorari to the Court of Appeals with regard to the denial of class certification (No. 81-2011). The Supreme Court, however, granted defendant Price Waterhouse's petition for a writ of certiorari with regard to the reversal of the grant of summary judgment.

As a result of the final denial of plaintiff's class motion, plaintiff is no longer in a position where she can represent a class. The amount of her individual claim is such that she can not justify incurring the further expense in pursuing the litigation. Even if the judgment of the Court of Appeals is affirmed by this Court, Mrs. Panzirer could not continue the litigation. Thus, whether the judgment of the Court of Appeals is affirmed or denied by this Court, Mrs. Panzirer can not continue to prosecute the action.

As this Court, and others, have recognized, denial of class certification is often the death knell of the litigation. *Eisen v. Carlise & Jacqueline*, 417 U.S. 156 (1974); *Eisen v. Carlise & Jacqueline*, 370 F.2d 119 (2d Cir. 1966), *cert. denied*, 386 U.S. 1035, (1967) (Eisen I); *Blackie v.Barrack*, 524 F.2d 891 (9th Cir. 1975).

It is certainly the death knell of this litigation as far as Mrs. Panzirer is concerned. Respondent Panzirer wishes to dismiss the action with prejudice. The effect of such a dismissal will be finally to determine this matter in favor of defendants and against plaintiff on all issues.[2]

Accordingly, Respondent Panzirer respectfully suggests that the cause is moot, and no longer a case or controversy, by reason of her determination not to prosecute the action and her desire to dismiss it with prejudice.

2. Mrs. Panzirer is prepared to pay the taxable fees and costs that may be due under the United States Supreme Court Rules.

The U.S. Constitution provides that the Federal Courts are vested with jurisdiction only over "cases" and "controversies". Article III, Sec. 2, The Constitution of the United States of America; *Flast v. Cohen*, 392 U.S. 83 (1968); *Poe v. Ullman*, 367 U.S. 497 (1961).

Where actions are moot they are no longer cases or controversies and must be dismissed. *United States v. Munsingwear*, 340 U.S. 36, 39 (1950) and cases cited herein; *Indianapolis School Commissioner v. Jacobs*, 420 U.S. 128 (1975); *Defunis v. Odeguard*, 416 U.S. 322 (1974); *Krumens v. Beatty*, 431 U.S. 119 (1977).

We respectfully request that the Court vacate the judgment below and remand with a direction to dismiss the action with prejudice.

Dated: New York, New York
August 6, 1982

Respectfully submitted,

s/ Daniel W. Krasner

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Opposition

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-v.-

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Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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81-1998

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PRICE WATERHOUSE,

Petitioner,

-v.-

ZELDA L. PANZIRER,

Respondent.

BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

The below-named respondents, who were among the defendants-appellees below, respectfully pray that, for the reasons set forth in Price Waterhouse's Petition for a Writ of Certiorari, said Petition be granted.

The decision below, *inter alia*, reversed the grant of the respective motions of Price Waterhouse and the below-named respondents dismissing the amended complaint. The below-named respondents' interest in the Petition is based on the fact (a) that their summary judgment motion was based on the same grounds as Price Waterhouse's motion, (b) that the two motions were treated together and granted by the District Court for the

same reasons and (c) that, similarly, the Court below treated the two motions together and reversed their grant for the same reasons.

Respectfully submitted,

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Petitioner's Reply Brief

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No. 81-1998

IN THE

Supreme Court of the United States

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PRICE WATERHOUSE,

Petitioner,

v.

ZELDA L. PANZIRER, et al.,

Respondents.

RESPONSE OF PETITIONER TO RESPONDENT'S SUGGESTION OF MOOTNESS

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IN THE

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PRICE WATERHOUSE,

Petitioner,

v.

ZELDA L. PANZIRER, et al.,

Respondents.

RESPONSE OF PETITIONER TO RESPONDENT'S SUGGESTION OF MOOTNESS

This memorandum is submitted in response to respondent's Suggestion that her own complaint should be dismissed as moot. Respondent's Suggestion of Mootness was filed shortly after this Court had granted certiorari to review the Second Circuit's judgment reversing the dismissal of respondent's complaint. In the unusual circumstances of the present case, where respondent seeks to withdraw her complaint and thus to abort the appellate process, petitioner submits that this Court, if it dismisses the writ of certiorari as moot, should (a) reverse the judgment below as moot, (b) remand with directions to dismiss the complaint with prejudice, and (c) specifically indicate that the judgment and opinion below should be accorded no precedential weight and should spawn no legal consequences.

Statement of the Case

The complaint was brought three years ago, against petitioner Price Waterhouse and others, on behalf of respondent Zelda Panzirer and a purported class of persons who bought the common stock of Allied Artists Industries, Inc. ("Allied") during the period from August 18, 1978 to April 4, 1979. Respondent purchased 500 shares of Allied's stock, at $7 per share, after reading an article in the *Wall Street Journal* while she was on an automobile trip to Vermont with her husband.

Respondent, originally the plaintiff, bases her Suggestion of Mootness upon the various decisions resulting in the denial of class certification in the present case. She asserts that as a result of those decisions, she "no longer has any substantial stake in the litigation" and "can not justify incurring the further expense in pursuing the litigation" (Suggestion of Mootness at 1, 2). In fact, the amount of respondent's individual claim has remained $3500 from the outset of the case, and the question of expenses never appears to have been a significant factor to respondent.*

This case has nevertheless been litigated with great vigor, at least until the present time. Over the past three years respondent's attorneys have, among other things, opposed motions to dismiss; undertaken discovery by interrogatories and depositions; drafted a 26-page amended complaint; moved for class certification; defended respondent in her deposition; opposed summary judgment motions; moved to reargue the denial of class certification; moved for certifica-

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* Respondent testified, at her deposition on November 6, 1979, that she had paid no monies to her attorneys in connection with this case, that she was not aware of anybody else making any such payments to her attorneys, that she recognized her obligation to pay certain costs if she lost the case, that she had no oral or written agreement to make any such payment, and that she had had no discussion about how the lawsuit was going to be financed.

tion of interlocutory issues to the Court of Appeals; defended against renewed motions for summary judgment; appealed from the grant of summary judgment and the denial of class certification; petitioned this Court for a writ of certiorari on the class action issue; and opposed Price Waterhouse's petition for certiorari on the merits of the case. Each of these matters involved substantial litigation time and expense; the docket sheet before the Court of Appeals was seven pages long.

On June 28, 1982, this Court granted Price Waterhouse's petition for certiorari to review the novel theory of Rule 10b-5 liability that the Second Circuit had adopted in reversing the District Court's dismissal of respondent's claim.* Concurrently, this Court denied respondent's petition for certiorari on the class action issues.

Having litigated the case vigorously for three years and having obtained a Court of Appeals decision that significantly extended the fraud on the market theory and the reach of Rule 10b-5 (as the Court of Appeals itself acknowledged, 663 F.2d at 368), respondent and her attorneys now seek to withdraw the claim and have it declared moot. In effect, they seek to prevent this Court from reviewing a ruling that they have fought for over three years to obtain, and that this Court has held to be appropriate for review.

This effort to withdraw does not stem from any non-litigation event. It stems, as respondent's Suggestion of Mootness indicates, solely from respondent's tactical litigation decisions.

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* The issue upon which the writ was granted was the following:

> "Can a Rule 10b-5 defendant, which has made an allegedly misleading statement relating to an issuer, be held liable to an individual who purchases the issuer's securities in the open market on the basis of comments 'heard on the street,' as reported in a newspaper article that refers to the issuer but not to the defendant, the defendant's statement or any facts set forth therein?"

Reasons for Reversing the Judgment Below

A. Summary of Analysis

Respondent and her attorneys seek to abandon the present case without permitting this Court to rule on the substantial issue, presented by the opinion and judgment below, that led this Court to grant certiorari. Respondent concedes that if the Court dismisses the writ as moot by reason of respondent's calculated withdrawal, it should vacate the judgment below and remand with directions to dismiss the complaint with prejudice (Suggestion of Mootness at 3).

If the judgment below is merely vacated, however, the opinion below is likely to spawn adverse legal consequences, a result that this Court has expressly sought to avoid in other cases vacated as moot. The risk is particularly severe for petitioner because it is the defendant in a series of cases that are based upon complaints copied almost verbatim from the present complaint. Plaintiffs in those cases may well seek to invoke the opinion below as having substantial precedential weight.

The disposition sought herein—reversal rather than vacatur of the judgment below, and an express statement that the opinion below should be given no precedential weight—has been granted by this Court in prior cases. Such disposition would be particularly appropriate in the present case because it would cause no harm to respondent (who seeks to have her complaint dismissed in any event); because it would decrease substantially the likelihood of petitioner's suffering adverse legal consequences from the opinion below; and because it would decrease the incentive for litigants to manipulate the appellate and certiorari process by blocking the review of novel opinions that may have far-reaching impact.

B. The Court's Exercise of Its Supervisory Power in Prior Cases

The "established practice of the Court," in dealing with civil cases from the courts in the federal system which have become moot, is to "reverse or vacate" the judgments below and remand with directions to dismiss. *United States* v. *Munsingwear, Inc.*, 340 U.S. 36, 39 (1950). Where, as here, respondent has deliberately taken actions that led it to claim that its own case was moot, this Court has reversed rather than merely vacated the judgment below. *See, e.g., Heitmuller* v. *Stokes*, 256 U.S. 359, 362-63 (1921) (judgment of the Court of Appeals reversed and remanded when the plaintiff—defendant in error—took actions that mooted the appeal to this Court); *C. M. Patten & Co.* v. *United States*, 289 U.S. 705 (1933) (decree below reversed and remanded when the plaintiff, after having obtained a favorable result below, abandoned the suit in this Court*). *Compare Great Western Sugar Co.* v. *Nelson*, 442 U.S. 92 (1979) (judgment below vacated when the controversy had become moot by reason of events other than tactical decisions of the respondent); *County of Los Angeles* v. *Davis*, 440 U.S. 625, 634 (1979) (judgment below vacated when the controversy had become moot by reason of events other than tactical decisions of the respondent).

The power to reverse or vacate the judgments below, where the underlying claims have been mooted so as to prevent or preclude the exercise of this Court's jurisdiction, stems from this Court's broad supervisory power over the lower federal courts. *United States* v. *Munsingwear, Inc.*, 340 U.S. at 40-41. In exercising its supervisory power, the Court may make "such disposition of the whole case as justice may require," *Walling* v. *James V. Reuter, Inc.*, 321

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* R. Robertson & F. Kirkham, *Jurisdiction of the Supreme Court* § 280 at 509-10 and n.3 (1951), sets forth the facts in *Patten*.

U.S. 671, 676-77 (1944), and may enter "such order as is 'most consonant to justice in view of the conditions and circumstances of the particular case.' " *Heitmuller* v. *Stokes*, 256 U.S. at 362, *quoting United States* v. *Hamburg-Amerikanische Packetfahrt-A.G.*, 239 U.S. 466, 477-78 (1916). In particular, the Court may take such action as may be necessary to prevent the judgment below—if it is unreviewable because of mootness—"from spawning any legal consequences." *United States* v. *Munsingwear, Inc.*, 340 U.S. at 41.

Vacating the judgment below helps to prevent that unreviewable judgment from spawning any legal consequences, in part because " 'vacating the judgment of the Court of Appeals deprives that court's opinion of precedential effect . . . .' " *County of Los Angeles* v. *Davis*, 440 U.S. 625, 634 n.6 (1979), *quoting O'Connor* v. *Donaldson*, 422 U.S. 563, 577-78 n.12 (1975). However, as Justice Powell observed in his dissent in *County of Los Angeles* v. *Davis*, if the judgment of the court below is merely vacated and not reversed, the expressions of the court below on the merits "will continue to have precedential weight and, until contrary authority is decided, are likely to be viewed as persuasive authority if not the governing law" of the circuit. 440 U.S. at 646 n.10.

The concern about the lower courts' treatment of vacated opinions is real and significant. For example, the Second Circuit, which rendered the judgment and opinion below, gave full precedential effect to its decision in *United States ex rel. Johnson* v. *Chairman, New York State Board of Parole*, 500 F.2d 925 (2d Cir. 1974), even though the judgment therein had been vacated as moot by this Court. 419 U.S. 1015 (1974). *See Coralluzzo* v. *New York State Parole Board*, 566 F.2d 375, 378 (2d Cir.), *cert. granted*, 434 U.S. 996 (1977), *cert. dismissed*, 435 U.S. 912 (1978).

Another example is *Davis* v. *Alabama*, 596 F.2d 1214 (5th Cir. 1979), *vacated as moot*, 446 U.S. 903-04 (1980). At least two lower courts have followed the Fifth Circuit's opinion in *Davis* as the most pertinent statement of the governing law, even though they recognized that this Court's vacatur of the judgment as moot had "technically" stripped the opinion of any precedential value. *See Voyles* v. *Watkins*, 489 F. Supp. 901, 910 and n.5 (N.D. Miss. 1980); *Blake* v. *Zant*, 513 F. Supp. 772, 780 and n.3 (S.D. Ga. 1981).

C. Reasons for the Court to Exercise Its Supervisory Power in the Present Case

In view of the treatment of vacated judgments by the Second Circuit and other lower courts, we respectfully submit that mere vacatur would provide inadequate protection for the petitioner in the present case and an inadequate safeguard for the appellate and certiorari process. Reversal rather than vacatur, coupled with an admonition against giving precedential weight to the judgment below, is amply warranted.

The need for such action by this Court results from respondent and her attorneys' taking a $3500 claim, litigating it to the hilt for three years, obtaining an unprecedented appellate opinion that warranted this Court's review, and then taking deliberate action to block that review and to leave outstanding an appellate opinion that would have no effect on respondent (who seeks to withdraw her claim with prejudice), that would be likely to have pernicious effects on petitioner and other Rule 10b-5 defendants, and that might well have beneficial effects for respondent's attorneys in future cases.* We submit that in these circumstances the

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* This Court referred, in *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 739 (1975), to the possibility that unduly extensive

(footnote continued on following page)

Court should exercise its supervisory authority to prevent abuses and inequities arising from tactical manipulation of the appellate and certiorari processes, and should take steps to assure that no significance will be attached to the opinion below.*

In seeking such action by the Court, we note that the existence of the judgment and opinion below threatens particularly serious legal consequences to the petitioner. The complaint in the present case, alleging that the financial statements contained in Allied's 1978 Annual Report were false and misleading, has already been copied almost verbatim in four other actions brought under Rule 10b-5. If the judgment below is not reversed, the courts in dealing with various aspects of such cases may well invoke the Second Circuit's unreviewed opinion and the novel theory of fraud on the market liability that it espouses.

Absent an explicit indication by this Court that the opinion of the Second Circuit is to be given no precedential weight, petitioner may, as a practical matter, be prevented from rearguing the legal inappropriateness of the opinion, for at least two reasons. First, the workload of the federal judiciary and other factors substantially reduce the time available for the critical evaluation of opinions already

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(footnote continued from preceding page)

imposition of civil liability under Rule 10b-5 " 'will lead to large judgments, payable in the last analysis by innocent investors, for the benefit of speculators and their lawyers' "; the Court also noted the "widespread recognition that litigation under Rule 10b-5 presents a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general."

* *See Walling* v. *James V. Reuter, Inc.*, 321 U.S. 671, 675, 677 (1944), vacating the Court of Appeals' judgment and restoring the contrary judgment of the District Court because respondent's action to moot the case had "rendered abortive" the appellate procedure and "frustrated" review by this Court.

issued by the circuit courts, unless readily demonstrable and obvious reasons exist to do so. A reversal of the judgment below, coupled with an express statement by the Court regarding precedential weight, should greatly increase the likelihood that the lower courts would undertake such an evaluation, and should thus give petitioner a realistic opportunity to argue against the reasoning of the court below.

Second, if companion cases to the present one were ordered to go forward on the basis of the theory advanced by the court below, the orders would not be reviewable on appeal (absent certification under 28 U.S.C. § 1292(b)) until after the cases had been fully tried. Petitioner would thus have to undergo the expense and effort of full-dress trials, over accounting issues that take up much of a 26-page complaint, before petitioner would have an opportunity effectively to challenge the unprecedented legal theory that this Court saw fit to review by its grant of the petition for certiorari herein.

In short, if the petition is merely dismissed and the judgment vacated as moot, the opinion below is likely to result in adverse legal consequences for petitioner. Reversal of the judgment below, rather than mere vacatur, should diminish the likelihood that this will occur. Other action by this Court to prevent the opinion below from spawning any legal consequences—such as an express statement that the opinion is not to be given precedential or persuasive weight—would also be appropriate, in order to effect "such disposition of the whole case as justice may require." *Walling* v. *James V. Reuter, Inc.*, 321 U.S. 671, 676-77 (1944).

Conclusion

For the reasons set forth above, petitioner Price Waterhouse submits that this Court, if it dismisses the writ as moot, should reverse the judgment of the court below, remand with directions to dismiss the complaint with prejudice, and take such other action as may be appropriate to prevent the judgment and opinion below from spawning any adverse legal consequences. As a matter of sound and fair judicial administration, this Court should take steps to assure that no advantage should be reaped by respondents, or lawyers, who seek to preclude the review of substantial issues by abandoning their claims after certiorari has been granted against them.

Respectfully submitted,

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No. 81-1998

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

PRICE WATERHOUSE,

Petitioner,

v.

ZELDA L. PANZIRER,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY OF RESPONDENT ZELDA L. PANZIRER REGARDING HER SUGGESTION OF MOOTNESS

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IN THE

Supreme Court of the United States

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PRICE WATERHOUSE,

Petitioner,

—*v.*—

ZELDA L. PANZIRER,

Respondent.

Respondent submits this memorandum to answer as briefly as possible Petitioner Price Waterhouse's diatribe denominated "Response To Repsondent's Suggestion of Mootness".

Petitioner has chosen, in the Supreme Court, to level baseless charges alleging "manipulation" of the judicial process by Respondent and her counsel. In effect, Petitioner urges that this Court punish Respondent and her counsel for seeking permission of this Court to dismiss the action and demand that this Court take the unprecedented step of indicating its views of the merits, without appropriate briefing or a hearing, concerning a matter which Petitioner concedes is moot.

Petitioner is incorrect on the law. Petitioner has also misstated the facts that it urges require the unique relief it demands.

Respondent indicated in the District Court and again in the Court of Appeals that denial of class certification would be the "death knell" of this action. Petitioner nevertheless argued that class certification be denied. Having succeeded, Petitioner now claims surprise when Respondent seeks a dismissal because it is financially unrealistic for her to proceed on an individual basis.

Without providing any specifics, Petitioner also suggests that there are pending related actions which would be affected by the *Panzirer* opinion. Petitioner, however, does not disclose the disposition of those cases. The record shows that in two of those

cases Petitioner consented to judgment for the individual plaintiffs and deposited the amount of the judgment with the Court. The third case, we are advised, has been settled, at least in part.

For over three years Petitioner sought and finally won a victory in this case; class certification has been denied.

With the final denial of class certification the posture of the case changed dramatically. In a class action context Plaintiff-Respondent was ready to press the litigation on behalf of the class and could expect to recover her costs, expenses and attorneys' fees if the action was successfully concluded. The economic risk was acceptable. Denial of class status left Respondent to prosecute her claim individually, without the benefits of class action procedures. The costs of such a prosecution, not including attorneys' fees, would exceed by many times the totality of Respondent's damages and they are not generally recoverable.

Although the Second Circuit has upheld her claim against Petitioner's motion for summary judgment, Respondent's damages simply cannot justify the expenses of further litigation. It makes no sense economically for Mrs. Panzirer to continue the suit.

Petitioner says that reversal is just punishment for alleged manipulation of the appellate and certiorari process.* This charge is baseless. Respondent cannot drop this case alone. She seeks this Court's permission.

Respondent's request for permission to dismiss the case results directly from the denial of Respondent's independent petition for a writ of certiorari.

Vacating the decision of the Court of Appeals deprives it of precedental effects. *County of Los Angeles* v. *Davis*, 440 U.S. 625, 631 (1979), a case relied on by Petitioner. Nevertheless, Petitioner demands, in effect, an unprecedented statement by this Court on the merits. In not a single case referred to by Petitioner

* Petitioner forgets that it offered to pay Respondent's claim after her appeal was filed because it sought to avoid review of the District Court's now rejected opinions.

did this Court do anything approaching what Petitioner suggests this Court should now do. The cases simply cannot be read to support Petitioner.

Indeed, the cases support the position of Respondent. Where a case has been mooted this Court will take such action as will preserve the rights of the prevailing party, either vacating, or reversing, as appropriate. Here, vacating the decision of the Second Circuit, reversing the grant of Petitioner's motion for summary judgment, and re-establishing the *judgment* of the district court in favor of Petitioner provides complete relief to Petitioner. In *Walling* v. *Reuter*, 321 U.S. 670 (1944), a case cited by Petitioner, this Court vacated the judgment of the Court of Appeals and restored the judgment of the District Court, where the appeal had been mooted because the respondent corporation was dissolved. Thus, Petitioner's strained interpretation of the cases is not reflective of the decisions themselves.

Respondent respectfully requests that she be permitted to dismiss this case and that the judgment below be vacated and the judgment of the District Court in favor of Respondent restored.

Respectfully submitted,

.....

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IN THE

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OCTOBER TERM, 1981

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ZELDA L. PANZIRER,
Respondent.

BRIEF OF AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS AS *AMICUS CURIAE* IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

The question presented by the Petition for a Writ of Certiorari may be reformulated as follows:

> Should an accounting firm that has examined the financial statements of an issuer be liable under Rule 10b-5 to a purchaser of such issuer's securities when the purchaser admits that she has not actually relied upon the allegedly misleading financial statements but has relied instead upon a newspaper columnist's discussion of a broker's comment regarding the issuer's future prospects?

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-1998

PRICE WATERHOUSE,

Petitioner,

v.

ZELDA L. PANZIRER,

Respondent.

BRIEF OF AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS AS *AMICUS CURIAE*

PRELIMINARY STATEMENT

The American Institute of Certified Public Accountants ("AICPA" or the "Institute") submits this brief as *amicus curiae*, pursuant to Rule 36.1 of the Rules of this Court,[1] and urges this Court to grant the Petition for a Writ of Certiorari filed herein. On Apirl 28, 1982, Petitioner timely filed the Petition for a Writ of Certiorari with this Court. This brief *amicus curiae* has been filed within thirty days of that date.

[1] This brief is submitted upon consent of the parties. The written consents of Petitioner and Respondent by their respective counsels are being filed contemporaneously with this brief.

OPINIONS BELOW

The opinion of the Court of Appeals, reported at 663 F.2d 365 (2d Cir. 1981) *sub nom. Panzirer* v. *Wolf*, is set forth in the Appendix to the Petition for a Writ of Certiorari ("App.") at 1a-9a. The opinions of the United States District Court for the Southern District of New York, reported at [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,363 and (CCH) ¶ 97,251 (S.D.N.Y. 1980) are also set forth in the Appendix at App. 16a-37a and App. 40a-49a.

INTEREST OF THE INSTITUTE AS *AMICUS CURIAE*

The Institute is a national accounting association, all of whose approximately 182,000 members are certified public accountants. Among the Institute's purposes are the promotion and maintenance of high professional standards of practice and, in the pursuit of those ends, the Institute has come to be accepted as the authoritative source of standards and procedures in its field. More particularly, the Institute formulates the auditing standards deemed "generally accepted" by the profession. One of these standards, the "going concern" qualification to an auditor's opinion, is involved in this litigation.[2]

As the issuer of these standards, the Institute has a profound interest in the scope and bases of civil liability, sought to be imposed on auditors in connection with their performance of engagements governed by such standards, under the rubric of Section 10(b) 15 U.S.C. 78j(b) (1976) of the Securities Exchange Act of 1934, 15 U.S.C. § 78a *et. seq.* (1976) ("Section 10(b)" and the "1934 Act") and Rule 10b-5, 17 C.F.R. § 240.10b-5 (1981) ("Rule 10b-5") promulgated thereunder.

Accordingly, the Institute was invited to and did submit a position paper to the United States Senate concerning the scope of civil liabilities and damages to be included within the

[2] *See Statement on Auditing Standards No. 34, The Auditor's Considerations When a Question Arises About an Entity's Continued Existence* (AICPA: March 1981).

Securities Exchange Act of 1934. *See Hearings on S. Res. 84 (72d Cong.), S. Res. 56 and S. Res. 97 (73d Cong.) Before the Senate Committee on Banking and Currency,* 73d Cong., 1st Sess., pt. 15, at 7207-10 (1934) (the "1934 Hearings"). Furthermore, this Court has permitted the Institute to file briefs *amici curiae* on related issues in *Ernst & Ernst* v. *Hochfelder,* 425 U.S. 185 (1976); *Touche Ross & Co.* v. *Redington,* 442 U.S. 560 (1979); and *Aaron* v. *Securities and Exchange Commission,* 446 U.S. 680 (1980).

In this case, the Court of Appeals for the Second Circuit has proceeded to reformulate and sharply reduce the quantum of reliance traditionally required by Section 10(b) and Rule 10b-5 for a purchaser or seller of securities to maintain a private cause of action implied under that section and rule.

The implications of the result below and of the unsatisfactory analysis adopted by the court transcend the interests of the parties litigant and raise significant and profoundly disturbing issues for the accounting profession as a whole, as well as for others who provide services to issuers and other participants in securities and financial transactions. The Institute here contends that those implications are neither required nor permitted by any correct reading of Section 10(b) or Rule 10b-5.

SUMMARY OF ARGUMENT

Definition of the contours of the private cause of action implied under Section 10(b) of the 1934 Act and Rule 10b-5 requires analysis of the language of the statute and its related sections and of the legislative history. Without undertaking such an analysis, the court below held that an accounting firm may be held liable under the securities laws to an investor who purchased shares of stock on the basis of a newspaper columnist's discussion of a broker's comment upon the issuer's intended entry into a new and expanding market. In so ruling, the court attempted to find reliance merely on the assertion that if the prior financial statements had been accurate, the broker or even the columnist might not have reported so favorably on the issuer's future prospects.

Analysis of Congressional intent through the words employed by Congress and expressed in the legislative history, however, demonstrates that the purported reliance theory adopted by the court below is wholly at odds with the type of reliance intended by Congress as prerequisite to civil liability for damages.

The failure of the court below to ascertain and follow Congressional intent by expanding the private cause of action under Section 10(b) and Rule 10b-5 gravely concerns the Institute. Of equal concern is that the decision also raises profoundly disturbing questions about the basis on which accountants are to be liable under Rule 10b-5. The speculative nature of an inquiry into whether the broker would have reported differently or the columnist would have written a different column had certain facts been disclosed is highly disturbing and invites disquieting inquiry into these complex issues by permitting interrogation of members of the press. Resolution of these issues requires an analysis ignored by the court below. The result reached by such examination militates against adoption of the theory accepted below and requires consideration of these issues by this Court.

REASONS FOR GRANTING THE PETITION

A.

THE HOLDING BELOW CONFLICTS WITH CONGRESSIONAL INTENT AS ESTABLISHED THROUGH APPLICATION OF GOVERNING PRECEDENTS OF THIS COURT

This Court is now called upon to shape still another contour[3] of the private cause of action for damages implied under Section 10(b) of the 1934 Act and Rule 10b-5. That

[3] The importance of these contours cannot be understated. In the words of this Court, per Justice Frankfurter addressing a similar analytical setting:

> To say that a man is a fiduciary only begins analysis; it gives direction to further inquiry. To whom is he a

process was begun in *Superintendent of Insurance* v. *Bankers Life and Cas. Co.*, 404 U.S. 6 (1971) and continued in *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972), *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185 (1976), *Piper* v. *Chris-Craft Industries Inc.*, 430 U.S. 1 (1977), *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462 (1977), *Touche Ross & Co.* v. *Redington*, 442 U.S. 560 (1979), and *Aaron* v. *Securities and Exchange Commission*, 446 U.S. 680 (1980). Here the issue focuses upon the nature of the requisite proof of reliance in a Rule 10b-5 case and the extent to which such reliance may be shown—not by reliance on the allegedly misleading financial statements themselves, but by reliance on the comments of a broker discussed in a newspaper column predicting future profitability of a new line of business.

Implication of a private cause of action in damages under Section 10(b) and Rule 10b-5 to create liability on the basis of such a purported causal nexus finds no warrant in the provisions of the 1934 Act. The statute itself indicates that civil liability in damages with respect to misleading documents filed with the SEC should not be created in favor of anyone who bought or sold a security without having relied upon those documents. The legislative history persuasively confirms that Congress did not intend the construction advanced by the court below. It further shows that Congress, as part of its regulatory scheme, carefully circumscribed private rights of action in a fashion precluding the claims asserted here.

(i) The Text of the Statute Demonstrates Congressional Intent to Circumscribe Narrowly Civil Liability in Damages on a Showing of Reliance Far Stronger than that Adopted by the Court Below.

In implying a cause of action under the federal securities laws, this Court has reiterated that "[t]he starting point in

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(Footnote 3 continued)
fiduciary? What obligations does he owe as a fiduciary? In what respect has he failed to discharge these obligations? And what are the consequences of his deviation from duty?

Securities and Exchange Commission v. *Chenery Corp.*, 318 U.S. 80, 85-86 (1943).

every case involving construction of a statute is the language itself." *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 756 (1975) (Powell, J., concurring). *See also Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 568 (1979); *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 472 (1977); *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 197 (1976). This textual emphasis does not concentrate upon the words of a particular section alone, admittedly powerful in and of themselves, *see Santa Fe Industries*, 430 U.S. at 477 and *United States* v. *Oregon*, 366 U.S. 643, 648 (1961), but rather gains definition from the statute taken as a whole. *See Touche Ross* v. *Redington*, 442 U.S. at 571; *Blue Chip Stamps*, 421 U.S. at 736.

The derivative "reliance" accepted by the Court below enjoys no support in the language of the statute and is inconsistent with the express statutory provisions that do require reliance. Thus, Section 18(a) of the 1934 Act, 15 U.S.C. §78r(a) (1976) ("Section 18(a)"), in which Congress created an express cause of action conditions liability for documents containing misleading statements of material fact filed with the Securities and Exchange Commission (the "SEC") upon proof that the plaintiff "who in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement . . ." *Ibid.*

This " 'double-barreled' causation requirement,"[4] expressed by Congress in Section 18(a), conveys no indication that Congress had any intention of creating an express remedy upon a lesser showing of causation.

In the case of an implied cause of action, such as Rule 10b-5, the result should be no different, absent contrary Congressional intent expressed in the text or legislative history of Section 10(b). But they indicate otherwise. The language of Section 10(b) says nothing in support of watering down or negating a reliance requirement. Reliance and scienter are the

[4] *Rich* v. *Touche Ross & Co.*, 415 F. Supp. 95, 103 (S.D.N.Y. 1976).

hallmarks of fraud[5] and, as this Court took pains to explain in *Hochfelder,* 425 U.S. at 198, 212 n.32, after an examination of the legislative history of Section 10(b), manipulation, deception and contrivance as utilized in Section 10(b) are active terms, implying actual deception. Those terms convey no suggestion to lessen the traditional burden of proof of fraud by watering down reliance.

Here, however, plaintiff claims reliance on the theory that the broker might not have reported so favorably on the issuer's future prospects had he known the existence of the alleged false and misleading statements and omissions in the financial statements or that, even more speculatively, the columnist might not have given the same play to the broker's comments. These assertions would not satisfy the second causal requirement enunciated by Congress in Section 18(a), involving an effect on price, much less the first. Indeed, the Court below reasoned that the plaintiff's "knowledge of the price of the stock and her conversation with her broker were merely neutral factors as they presented no impediment to her acting on the favorable notice in The Wall Street Journal." (App., at 6a). It underscored this point by adding:

> Plaintiff refers to the price of Allied common stock once in her deposition: "If the price was outrageous, something very high, I wouldn't have been interested. The price was attractive." If anything, her testimony indicates that a lower price accurately reflecting Allied's true financial position might have led her to buy more stock.

(App., at 6a, n.3).

Secondly, it is beyond cavil that the first of these Congressionally articulated requirements, actual reliance on the misleading statement, is not satisfied here. Although this Court in *Affiliated Ute* created a presumption of actual reliance in a case involving face to face transactions, fiduciary relationships and

---

[5] *See Restatement of Torts* § 525 (1938).

"primarily a failure to disclose", *id.*, 406 U.S. at 153, the District Court below expressly found—and the Court of Appeals did not disturb the finding—that "any presumption that plaintiff relied upon the alleged misrepresentations or omissions in Allied's 1978 Annual Report" had been rebutted by plaintiff's own assertions. (App., at 46a).

The holding below thus strays far beyond the confines that Congress set in enacting a comparable course of action. Yet this Court has cautioned that

> [W]e are extremely reluctant to imply a cause of action [in one section of the 1934 Act] . . . that is significantly broader than the remedy that Congress chose to provide [in another section]. *Blue Chip Stamps* v. *Manor Drug Stores, supra,* at 735-736; see *Ernst & Ernst* v. *Hochfelder, supra,* at 210; *Securities Investor Protection Corp.* v. *Barbour, supra,* at 421-423; *Amtrak, supra,* at 458; cf. *T.I.M.E. Inc.* v. *United States,* 359 U.S. at 471.

Touche Ross, 442 U.S. at 574. (Footnote omitted).

The same holds true in interpreting the language of Section 10(b). It should not be construed to imply a cause of action so "significantly broader than the remedy that Congress chose to provide." *Ibid.*

(ii) The Legislative History: Congress Did Not Intend Civil Liability in Damages on the Basis of the Purported Reliance Theory of the Court Below.

The legislative history affords no basis for such an implication and demonstrates that the requirement of actual reliance is a part of Section 10(b) and the statute as a whole. As the Senate committee report on the 1934 Act states, the purchaser or seller must "show the violation or the fact that the statement was false or misleading, *and that he relied thereon to his damage.*" S. Rep. No. 792, 73d Cong., 2d Sess. 12-13 (1934), *quoted in Ernst & Ernst* v. *Hochfelder,* 425 U.S. at 206 (emphasis added).

The requirement of actual reliance is, if anything, plainer with regard to Section 18(a) where, unlike Section 10(b), Congress expressly provided for a private cause of action. Both the Senate Report[6] and the House Report[7] regarding Section 18(a) affirmed that liability in damages with respect to misleading statements contained in filed documents lies in favor of "a person who in reliance on the statement and in ignorance of its false or misleading character has purchased the security to which it relates at a price affected by it." H. R. Rep. No. 1383, 73d Cong., 2d Sess. 25 (1934). Moreover, as the Senate Report added, "the burden is on the plaintiff to show . . . the fact that the statement was false or misleading, and that he relied thereon to his damage." S. Rep. No. 792, 73d Cong., 2d Sess. 13 (1934).

This uniformity of Section 18(a) speaks not of an indifference by Congress regarding potential liability to anyone who may read a newspaper column about a company's new products being in demand in an expanding market, but rather of a conscious intent to restrict such liability. An earlier version basing liability only upon the absence of good faith and proof that the stock price was affected by a misstatement was "very much challenged on the ground that reliance should be required." 78 Cong. Rec. 7701 (1934). This circumscribed formulation was insisted on, for example, by Chairman Rayburn of the House Committee on Interstate and Foreign Commerce in explaining the very bill he sponsored:

> Mr. Hollister. The gentleman keeps referring to the issuer or the seller. This is a general clause and covers anybody making any kind of statement in any kind of document or in any kind of paper that is filed. It includes accountants, lawyers, or any other expert.
>
> [A request of additional time was made]

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[6] S. Rep. No. 792, 73d Cong. 2nd Sess. 21 (1934).
[7] H.R. Rep. No. 1383, 73d Cong., 2nd Sess. 25 (1934).

> Mr. Rayburn. I want to read this part of the section to the gentleman:
>
> Who, in reliance upon the statement, shall have purchased or sold a security.
>
> Mr. Hollister. Yes; that is the man who is going to sue. I am talking about the report that is made. This refers to any statement that is made in any report under this bill, if it contains a misleading statement.
>
> Mr. Rayburn. If upon that report somebody bought or sold a security and lost money relying upon the statement that was false.

78 Cong. Rec. 8040 (1934).

Even with these limitations, the drafters of the 1934 Act expressed the concern that Section 18(a) went too far. Thomas Corcoran, one of its authors, and others criticized its long period of limitations which gave rise to the possibility of "blackmail". 1934 Hearings at 6565. The Institute expressed concern about the amount of damages originally provided. *Id.* at 7207-10. These matters were addressed and the civil liability provisions of the 1934 Act and of the Securities Act of 1933, 15 U.S.C. § 77(a) *et seq.* (the "1933 Act"), were accordingly tightened. ***Blue Chip Stamps,*** 421 U.S. at 736, 740-41.

The decision below is thus not supported by the legislative history. It hardly accords with Congressional intent, as articulated by Mr. Rayburn, to hold an accountant liable, not on his "report", but on the basis of a newspaper columnist's opinion.

(iii) The Extrinsic Evidence From the Texts of Other Sections of the 1934 Act Shows the Error of the Holding Below

The interrelated nature of the various sections of the 1934 Act makes instructive an examination of the limitations on civil liability found in the 1934 Act. With respect to the "fraud on the market" theory employed by the Court below, Congress

addressed the issue of filed misleading statements in Section 18(a) and the issue of manipulation in Section 9 of the 1934 Act, 15 U.S.C. §78(i) (1976) ("Section 9").

It is clear from the language employed in Section 18(a) and its legislative history that Congress intended to preclude liability absent a strong showing of reliance. The holding below thus conflicts with this Court's holding in *Redington* that the language and intent of Section 18(a) are nearly conclusive in determining whether a civil cause of action in damages under the 1934 Act may be more broadly implied than that expressly set forth in Section 18(a).

This conclusion is further supported by the observation that when Congress intended to impose liability for false statements having market impact it knew how to do so and expressly limited the available relief. In Section 9(e), Congress expressly provided civil liability in damages for misleading statements having an impact upon the price of the security, but limited such liability in numerous ways.[8]

Here, however, the court below conceded that, had the financial statements in issue in this case not been allegedly misleading and the price for the securities been less as a result, the purchaser would not have been deterred and might merely have purchased more stock for the same amount of money. (App., at 6a, n.3). That concession is nothing less than a concession that the purchaser would not have a cause of action under Section 9(e).

To this anomaly is to be added the further irregularity that the persons subject to liability for fraud on the market under Section 9(e) are limited by Congress to actual participants in

[8] Section 9(a)(4) makes it unlawful for "a dealer or broker, or other person selling or offering for sale or purchasing" a security registered on a national exchange to make a misleading statement to induce the purchase or sale of that security. In Section 9(e) Congress provided for civil liability for violation of Section 9(a)(4) but created such a cause of action only in favor of those "who shall purchase or sell any security at a price which was affected by such act or transaction."

securities transactions. These carefully drawn limitations[9] would be negated by an interpretation of Section 10(b) to subject all those who merely file documents with the SEC and, like accountants, are associated with such documents, to civil liability in damages on the basis that a broker, interviewed by a columnist, would have changed his opinion and the columnist would not have so reported the broker's comments.

B.

THE DECISION BELOW RAISES DISTURBING POLICY IMPLICATIONS THAT SHOULD BE ADDRESSED BY THIS COURT

As if it were not disturbing enough for the court below to have distorted beyond recognition the type of reliance that Congress so plainly intended, its decision raises further disturbing implications arising from acceptance of the theory that the reliance of the media can be the reliance of a purchaser.

The widespread reporting by financial columnists in a variety of publications itself emphasizes the point. Presumably the investment choices of those who discuss the stock market in national publications and in local journals may all be the subject of an accountant's liability litigation every time an investor loses money from following a newspaper tip. The liability of accountants who earn nothing but a fee for their auditing work would therefore turn, in part, on brokers'

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[9] As originally enacted, Section 11 of the Securities Act of 1933, 15 U.S.C. § 77(k) (1976), provided a private right of action in damages to market buyers of registered securities where the registration statement contained a material untruth or omission without regard to reliance. However, in 1934 Congress further restricted that cause of action by requiring the purchaser to show reliance on the prospectus once an earning statement covering a period of at least twelve months had been made generally available to security holders. Pub. L. No. 291, 48 Stat. 907, 73d Cong., 2d Sess. (1934). Thus, Congress in 1934 restructured Section 11 to fit the reliance requirement of Section 18(a) of the 1934 Act which pertains to documents filed with the SEC.

opinions as discussed in the media, not the accountant's own work.

In fact, if the decision below remains uncorrected by this Court, that liability will turn on the basis of the type of speculation condemned by this Court in *Blue Chip Stamps.* There, this Court noted the highly speculative nature of the inquiry of whether a person would or would not have sold stock if certain facts had been revealed. *Id.,* 421 U.S. at 743-749.

In fact, the speculation will be more rampant in this case and the cases to come, if the theory adopted below is upheld. It can hardly be more speculative to request a columnist, after the event, to opine without the benefit of obvious hindsight as to what he would have written had he known any one of a number of facts pertaining to the subject of his column.

And the undertaking of that inquiry raises its own issues of journalistic confidentiality and protection of sources far more complex than those addressed by this Court in *Herbert* v. *Lando,* 441 U.S. 153 (1979), which permitted such inquiry in defamation cases. But in defamation cases, at least it can be said that the journalist is aware of the dangers and assumes the risk of malicious publication.

In cases such as the instant case alleging that the journalist would have written something different had he not considered the misrepresentation, no such risks were taken. Yet the media would presumably be subject to full examination and cross-examination of its knowledge, motives and intent—a course that can only chill the free flow of information.

What the court below did was to shift the inquiry under the securities laws from whether there were full disclosure to investors relying upon financial disclosure to a different kind of inquiry involving the market-place of ideas. No Congressionally articulated policy supports holding accountants liable on that basis or subjecting journalists to that inquiry.

This Court has frequently granted certiorari to review cases in which the issue was important to the administration of the

federal securities laws. *See, e.g., Santa Fe Industries, Inc.* v. *Green,* 430 U.S. at 471. When review was necessary to correct an important doctrinal problem, this Court has not hesitated to do so despite the non-finality of the judgment sought to be reviewed. *E.g., United Housing Foundation, Inc.* v. *Forman,* 421 U.S. 837 (1975).

The holding below raises sharp concerns requiring this Court's review at this stage. It contradicts the intent of Congress, expressed in Section 18(a) and in the legislative history of Sections 10(b) and 18(a), to allow recovery upon the purported showing of reliance theorized by the Court below, and it poses serious questions as to the basis for an award of civil liability damages and the social costs to be expended if that theory of reliance is permitted to stand.

CONCLUSION

For the foregoing reasons, the Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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